PDBCI 162
97623

United States Agency for
International Development
Senegal

Program Assistance Completion Report
African Economic Reform Program I
(685-0291)

Prepared by:PRM/AS:CCowey

Approved by:DDIR:DLSheldon

May 1994

TABLE OF CONTENTS

I. EXECUTIVE SUMMARY

The Senegal African Economic Policy Reform Program I (AEPRP I) was implemented from August 1986 to September 1993. It was among the first five of the Africa Bureau's policy reform programs introduced in 1985 to provide relatively quick disbursing, policy conditioned assistance to governments interested in undertaking fundamental economic reforms.

Funded through ESF, the $15 million program consisted of a $14 million cash transfer and a $1 million studies and technical assistance component. The program agreement was signed on 22 August 1986. Disbursement was made in three tranches, between September 1986 and December 1988. Two PACD extensions were issued, the last one in July 1991 agreeing to a terminal date of 30 September 1993 in order to pursue technical assistance activities.

The purpose of the program was to support a package of tax reforms being undertaken by the Government of Senegal (GOS) as part of its structural adjustment process, in the context of the New Industrial Policy.

AEPRP I-supported reforms were intended to:

-- remove disincentives to savings and productive investment by reducing customs tariffs and direct tax rates;

-- increase the equity of the tax system by widening the tax base and reducing tax evasion;

-- reinforce the overall economic reform effort, aiming to reduce government interventions and to provide incentives for growth of a vital and competitive private sector.

These objectives were pursued through the definition of ten conditions precedent to disbursement distributed over three tranches, the execution of a number of studies on the tax system leading to a major revision of the Senegalese income tax code, and the design and implementation of a system to monitor the impact of the reforms on the industrial sector. USAID/Dakar interest in income tax reform was pursued further through ESF VII (1989-94).

The AEPRP I program was subject to a RIG audit in 1988 and to an AID/W evaluation of the program's impact on the industrial sector in early 1990. In late 1991, a synthesis report for the program's monitoring component was prepared. Conclusions and recommendations of these reviews are provided in Annexes A, B, and C.

While in the short term the AEPRP I program produced the desired results of reducing barriers to trade (by lowering tariffs and

3

eliminating import quotas on most goods) and a new draft tax code, its medium term success in terms of encouraging development of a competitive private sector was jeopardized by the GOS failure to fully implement key accompaniment measures (especially vigorous and **equitable** private sector promotion and improvements in tax administration) that would have permitted firms to adjust to the onslaught of external competition. Furthermore, the generalized economic slump experienced by the economy during the implementation period (aggravated in 1988-89 by political instability) eventually resulted in the restoration of many tariffs to their pre-reform levels, as the program objective of widening the tax base failed to materialize and government revenues fell instead of increasing.

With the benefit of a longer perspective, nevertheless, it is clear that the policy dialogue generated with the GOS and other donors through this initial effort gradually led to recognition by the GOS of the role and importance of a competitive private sector in the economy. While the shock administered by the New Industrial Policy (as partially implemented) to the formal private sector may have been unintentionally severe, resulting in substantial loss of income and employment, it also provided an impetus to the growth of a vibrant informal sector and stimulated reflection on more fundamental issues of Senegal's economic development policy.

II. BACKGROUND

A. Program Context:

Twenty-five years after independence (1960) the Senegalese economy was experiencing major difficulties. These hardships were especially evident in the industrial sector, the object of heavy tariff protection and fiscal policies which heavily taxed both the agricultural sector and consumers alike. Senior members of the Government of Senegal (GOS) and major donors agreed that industrial sector policy reform in the context of a broad process of structural adjustment, begun five years earlier, constituted essential conditions for renewed economic dynamism. (Lowenthal et al., Tax Reform in Senegal, 1986-1990, January 1990)

The New Industrial Policy adopted by the GOS in 1986 and supported by the IMF, the World Bank, and France incorporated a comprehensive package of tax reforms, including:

-- revising the customs code and progressively reducing tariff rates over two years, as well as progressivelly removing quantitative restrictions on imports; technical assistance would be provided by France for customs computerization.

-- revising the investment code to eliminate many of the loopholes created by exemptions and exonerations;

-- reforming the structure and rates of the direct tax system

4

in order to move progressively toward a global, rather than a schedular, system. A reduction in marginal tax rates and improved tax administration were to enhance the equity of the system; and

-- putting in place a real estate cadaster in greater Dakar and other urban centers in order to facilitate property taxation -- an important element in expanding the tax base.

The medium term expectations of the Policy were to increase industrial sector flexibility and encourage competitiveness (through reduced protection and tax rates). Inefficient enterprises were expected to close, marginal ones to have access to sufficient incentives to recover, and strong, well-managed ones to expand. A more enabling environment would also encourage enterprise creation. The New Industrial Policy incorporated a proposal to make credits available for restructuring existing enterprises, to help viable enterprises weather the short term difficulties.

B. Program Structure:

AEPRP I disbursed three tranches of $5 million, $5 million and $4 million respectively in September 1986, September 1987, and December 198?, after the GOS had satisfactorily met the required conditions precedent. These conditions, three for the first two tranches and four for the last tranche, covered:

a) progressive decreases in tariff rates (tr. 1,2,3);
b) progressive removal of quantitative restrictions on selected products (tr. 1,2,3);
c) adoption of the new 1986 customs code (tr. 1);
d) continued activity of the GOS working group on tax reform, to draft a new Code moving toward a global income tax, reducing the marginal tax rate, and simplifying the system (tr. 2,3);
e) publication of a new Investment Code compatible with the new customs tariff regime.

In addition to the statutory covenants, the GOS agreed a) to report on progress in renegotiation of special agreements granted under the existing Investment Code and b) to provide evidence on implementation of the fiscal cadaster and examination of a new tax schedule for General Tax Code implementation.

The complementary project grant agreement of $ 1 million financed a number of studies and expert consultancies dealing with income tax reform and the drafting of a new income tax code. Technical assistance was also provided to assist the GOS in 1) establishing and implementing a monitoring system for industrial sector performance and 2) developing a tax administration training program.

Following USAID/Senegal practice at the time, local currency generated under the program was used to reduce GOS debt to the

Senegalese private sector.

An audit of the program was conducted by RIG/Dakar in July 1988, prior to third tranche disbursement, and an AID/W impact evaluation took place in early 1990. (The original evaluation was reissued as A.I.D. Impact Evaluation Report No. 77 by PPC/CDIE in September, 1990.) In late 1991, a synthesis report for the program's monitoring component was prepared.

III. Review of Program Achievements (Outputs)

A. Purpose:

The program reinforced the World Bank's actions in supporting comprehensive tax reform. As such, it was an extremely sensitive undertaking, as it involved not only risks to the government's revenue-generating mechanism but also implied basic changes in economic management. Indeed, an economy based on market competition is regulated much more through relatively automatic price mechanisms (exchange rates, tariffs) than through direct administrative controls (quotas, licenses). The purpose of the program was achieved in the short run. Despite medium-term reversals, the program was probably also instrumental in bringing about a strong enough challenge to the traditional "dirigiste" government mentality to lead to more comprehensive market liberalization measures in the longer term.

B. Objectives:

In the short term, the program's objectives were met. All conditions precedent were satisfied, and the expected changes in tax, tariff, and Investment Code measures put in place. The draft of the new, simplified income tax code was completed. The stage was set for a more equitable tax system and investment environment, reduced government intervention in the economy, and development of a competitive private sector.

The 1990 impact evaluation concluded that

> Although USAID/Dakar funds represented a small percentage of the resources estimated by the World Bank for industrial sector restructuring, USAID-financed reforms constituted the major economic and financial reforms implemented in the first phase of the NPI....

In retrospect, however it is clear that these achievements were not to be sustained, and some setbacks had already begun by the end of 1989. While making allowances for the fact that some of the reform's benefits would take time to unfold while negative effects such as enterprise closings and declining revenues were evident in the short term, the team also recognized that extraneous factors contributed in large measure to the lack of success:

> The designers of the reform program... did not predict the increase in administrative fraud, the impact of political instability, the impact of differing donor agendas and willingness to participate in the reform process, and the time required for a rigid and unadaptive industrial sector to respond to competitive pressures.

In fact, the "second phase" of the NPI, dependent largely on other donor and GOS action, never materialized. Failure to implement complementary measures such as customs enforcement, elimination of special investment "conventions" or of various tax exonerations, combined with insufficient tax revenues resulted in the reversal of tariffs to close to their pre-reform levels by 1991 (World Bank Macroeconomic Update, 1991, para. 40).

With respect to the objectives identified in the program documentation:

-- Widening the tax base (by reducing rates and improving tax administration): While the rates were reduced as specified in AEPRP conditionality, the critical element of improving tax administration did not materialize. This encouraged an increase in fraud and accelerated the reduction of government revenue.

-- Removing disincentives to investment (by lowering the rate of protection and administrative barriers): Among the principal barriers to investment by existing and new firms were the special "conventions" (preferential licensing agreements) and tax/tariff exonerations negotiated by certain firms. Merely adopting a revised Investment Code did not have an impact on preferential treatment, and thus the expected levelling of the playing field -- giving all firms similar opportunities -- did not occur. Similarly, well-connected firms were able to evade taxes and tariffs, increasing their advantage against less favored enterprises.

-- Reinforcing economic reform and providing incentives for growth of the private sector: It is evident from the above that very little occurred to increase the equity of the system, and that barriers to competitive private sector development were not effectively broken down. Indeed, with respect to reinforcing reform, one fundamental measure was deliberately not addressed: the issue of exchange rate valuation. The fact that Senegal belongs to a monetary union, and thus does not have direct control over its exchange rate, and the prevalent belief at the time that a well administered system of tariffs and subsidies could substitute for direct exchange rate management are key reasons that explain this omission.

Various analyses of the NIP have pointed out that years of protection had weakened the industrial sector's capacity to respond to competition and many firms were unprepared for the onslaught of inexpensive imports which flooded the market following tariff and quota reductions. At the same time, the critical accompanying components, outside the scope of the AEPRP program, were not implemented in a timely manner. As noted in the 1991 synthesis report:

-- customs administration reform was not phased in **before** the tariff changes, thus contributing to an increase in fraud;

-- changes to existing labor laws as well as adjustments to controlled input costs (especially energy) were delayed, adding to firms' difficulties in containing costs;

-- the line of credit destined to finance the restructuring of the industrial sector (the World Bank's APEX) was also made available much later than planned, and proved inadequate for the task it was to accomplish.

The shock administered by the New Industrial Policy to the formal private sector may have been unintentionally severe. In the formal sector, losses in production, income, and employment by the end of 1991 appeared to have outnumbered the gains in new activities. This trend, aggravated by continuing economic stagnation, has persisted. However, such a situation did provide an impetus to the growth of a vibrant informal sector and stimulated reflection by the donors and within the GOS on more fundamental issues of Senegal's economic development policy. By the time of the 1993 election year, private sector issues were being taken much more seriously by the GOS, and local private sector participants themselves -- industrialists as well as traders -- were gaining confidence in their position as key players in the economic growth of the country. The foreign exchange devaluation of 1994 only served to reinforce these tendencies.

C. Studies

1. In depth analyses of Senegal's income tax system and statistics were conducted to identify the likely impact of converting the existing schedular system (where different sources of income are taxed at different rates and with different exonerations) to a unified system which would be more transparent and easier to administer. Another major criterion of the reform was to ensure that no revenues would be lost following the change, even though the maximum marginal tax rate, 65 percent in 1986, was to be reduced. (Improved tax administration was to help fill the gap in the medium term, while short term support would be provided by donor budget assistance.) These analyses were used by a working group in the Ministry of Finance to produce the draft revised Tax Code.

2. The second major set of studies was done under the program's Monitoring and Evaluation component. They focused on following the evolution of a sample of industrial sector firms (covering on average 50-55 percent of sector employment) as the impact of the reforms took hold. The firms were distributed among four representative sub-sectors: food processing, textiles, chemicals, and intermediate goods. Data was collected quarterly, on the basis of a survey instrument specially designed by project contractors, and entered into a specially designed computerized system managed by the Forecasting and Statistics Office of the Ministry of Plan (later Finance). Periodic reports were issued for each major sub-sector. The synthesis report for this set of studies was completed in October 1991.

On the basis of the data collected through the monitoring system, the report came to the surprising conclusion that, through 1988, about as many industrial branches had experienced an increase in the effective rate of protection as had experienced a decrease. (Based on the vocal protests lodged against the New Industrial Policy, one would have expected that far more had been hurt.) For 1989, however, and probably before the effects of the tariff increases of that year were reflected in the data, only one-fifth of the industries surveyed showed such an increase, and one-sixth showed no significant change from 1986. Again, only half of the industries had experienced a decrease in protection.

IV. Program inputs

A. Cash grant disbursement

Disbursement of the grant was made in three tranches of $5 million, $5 million, and $4 million respectively in September 1986, September 1987, and December 1988, after the GOS had satisfactorily met the required conditions precedent. Local currency counterpart funds were deposited in a special bank account and used, by mutual agreement between USAID and the GOS, to reimburse GOS arrears to small and medium sized businesses and local banks holding debt of the liquidated ONCAD parastatal. The RIG audit report of July, 1988, found that several of these payments, amounting to about 6 percent of the first tranche local currency equivalent, could not be verified. The report stated that while auditors uncovered "no evidence of diversion or unauthorized use of local currency, the potential for abuse is increased when there is little information to adequately identify payees". As a result, the Mission issued a policy directive detailing procedures for payment of local currency debts which would establish a system of sample testing to better ensure that future counterpart funds would be used for intended purposes. In subsequent Cash Grant programs, the Mission substituted a system of reimbursing the GOS for repaying its debts, rather than authorizing direct repayments.

B. Technical assistance

In addition to funding the studies identified above, this component provided expert assistance in designing the industrial sector survey, establishing a computerized data management system, and training GOS staff to analyze its results. In the tax administration area, USAID/Dakar entered into a PASA agreement with the U.S. Internal Revenue Service, under which IRS training specialists worked with the GOS Tax Department to provide advice on property taxation and to establish an in-house tax administration training program.

The Completion Date of the AEFRP I program was extended to September 1993 in order to permit continued technical assistance to the Tax Department.

C. Commodities

Computer equipment was provided to the Statistics Department to permit the compilation and analysis of the industrial survey data. Computer equipment was also provided to the Tax Department in support of the long-term tax administration training activity flowing out of the technical assistance of AEPRP I, but directly funded under the ESF VII program.

V. Lessons Learned

USAID agreed to take responsibility for one component of a multi-donor program. USAID successfully negotiated tax reforms agreed to by all the donors, and monitored their implementation by the GOS. However, other complementary reforms and support measures critically linked to the success of the tax reforms but depending on **other donors** for their implementation were not fully implemented. The commitment of other donors in a multi-donor effort should also be negotiated and monitored, to the extent possible.

Competing donor agendas interfered with the full implementation of the New Industrial Policy, and combined with other external factors to result in medium-term reversal of some of the tariff reduction measures supported by AEPRP I. Greater USAID sensitivity to these competing agendas could have helped identify, and possibly mitigate, their potential negative impact on the overall reform.

USAID changed its practices for local currency use in order to establish stronger controls on the ultimate use of funds.

Annex A

RIG Audit of AEPRP I: July 19, 1988

SUMMARY

The Office of the Regional Inspector General for Audit, Dakar, conducted a program results audit for the period August 1986 through April 1988, to (1) assess the adequacy of the USAID/Senegal system for measuring program effectiveness, (2) determine the extent to which the program had achieved desired results, and (3) identify factors inhibiting performance.

The audit found that USAID/Senegal had established an adequate monitoring and evaluation plan to measure program effectiveness. However, macroeconomic results of reforms been made later in the program were not expected until some time after the project ended. The Mission had also adequately monitored GOS actions to meet the Program Agreement conditions precedent for the two tranches already released.

The audit identified a weakness in USAID/Senegal monitoring of the use of local currency, finding that several payments claimed by the GOS could not be verified. The Mission relied on listings of payments provided by the GOS without independently verifying that payments had actually been received. The audit recommended additional verification procedures in the form of a system of sample testing, to better ensure that local currency was used as intended.

In replying to the draft audit report, the Mission stated that they had issued a policy directive detailing procedures for testing actual receipt of payments from the GOS to beneficiaries. The Mission also requested the GOS to provide information on the unconfirmed payments in the audit sample. Thus, RIG's recommendation was considered as closed upon the issuance of the report.

ANNEX B

IMPACT EVALUATION SUMMARY

Summary

The Agency for International Development's (A.I.D.) African Economic Policy Reform Program (AEPRP-I)[1] in Senegal was designed to play a supportive role to the industrial sector reforms managed by the World Bank. The World Bank initiative targeted a wide range of policy and institutional reforms to promote increased economic activity, more stable government revenues, and greater public sector effectiveness. The AEPRP-I reforms targeted tax and revenue administration. This report presents new data to demonstrate the impact of the AEPRP-I reforms, the methods and analysis used to distinguish actual impacts from exogenous factors, and the lessons learned in promoting industrial restructuring through tariff and tax reform in Senegal.[2]

By the mid-1980s, Senegal was experiencing major economic difficulties—difficulties that were especially evident in the industrial sector. Because of years of heavy tariff protection and fiscal policies that heavily taxed the agricultural sector and consumers alike, the industrial sector became stagnant. Government revenues from productive economic activity declined, and the economic costs of industrial protection became unsustainable. Faced with the gravity of the crisis, senior members of the Government of Senegal and major donors agreed that industrial sector policy reform in the context of broad structural adjustment was essential for renewed economic dynamism.

Based on this assessment the Government and the donor community identified a wide range of industrial sector policy reforms, which collectively became known as the New Industrial Policy or Nouvelle Politique Industrielle (NPI). A.I.D.'s AEPRP-I played a secondary, reinforcing role to the NPI reforms.

A.I.D. contributed $14 million in cash transfer funds (which generated an equivalent sum of local currency) and $1 million in technical assistance to promote the AEPRP-I reforms. Although A.I.D. funds represented only a small percentage of the total resources required for the industrial sector restructuring, the AEPRP-I comprised the major economic and financial reforms implemented during the first phase of the NPI (1986-1990). In many respects, AEPRP-I functioned substantively as the NPI during this period—a fact that prompted the evaluation team to consider the AEPRP-I reforms in the context of the NPI, even though A.I.D. never anticipated this scope for its policy reform framework.

Almost all of the economic policy reforms targeted by A.I.D. were implemented over a 3-year period, from 1986 to 1988. During this period, the Government of Senegal substantially reduced quantitative restrictions on imports, allowing commercial and industrial actors broad import authority; implemented a new commercial investment code; reduced across-the-board-tariff protection; and designed a dramatically revised tax revenue system that included major provisions for taxing urban real estate. A.I.D. and the Government of Senegal believed that these reforms would broaden the tax base, increase incentives for productive investment, increase Government tax

[1] A.I.D. has implemented two economic policy reform programs in Senegal: Industrial Sector Reform (AEPRP-I) and Financial (banking) Sector Reform (AEPRP-II).

[2] CDIE Working Paper No. 135 contains a longer version of this paper and the complete appendixes.

revenues, and increase the competitive capacity of the industrial sector.

However, by early 1990, none of these objectives had been attained. Stiff fiscal reform measures, increased external competition, and new administrative procedures require near-term adjustments whose positive effects may not become apparent until the medium term. Furthermore, Senegal's economic environment was extremely unfavorable to reform attempts.

Available data, review of recent donor analyses of industrial sector performance, and interviews with a wide range of actors in the public and private sectors, both formal and informal, indicate that the tariff reduction and import liberalization introduced in 1986 and 1988 did produce a psychoeconomic shock to the industrial sector. Accustomed to decades of protection, in some cases predating independence, private firms had made no provisions for competing in an international market. The immediate impacts of the policy reforms were a slowdown in economic activity in the formal industrial sector and a serious reduction in Government revenues. But these adverse impacts were only partially related to the reforms.

In fact the major reasons for the slowdown in formal sector activity are much broader than the relative reduction in tariff protection. The main attacks on industrial competitiveness came from the unexpected increase in administrative fraud following the reduction in customs rates. Import liberalization attracted short-term profit-seeking individuals, many with little or no previous commercial experience in the formal sector, who imported huge quantities of finished goods. Importers declared these goods at values so unreasonably low as to negate fully any remaining tariff protection for the higher priced domestically produced goods. While the evaluation team was unable to estimate the degree of this fraud, information gathered from multiple sources confirms the negative impact of administrative fraud on formal sector activity.

Another factor decreasing the competitiveness of domestic producers in the formal sector was the weakening purchasing power of the Senegalese economy. The decline in purchasing power showed a historical trend in Senegal, having dropped by approximately 50 percent since 1960. This decline accelerated in 1988-1989 because of political instability, an unexpectedly low peanut harvest, locust infestations, and the adverse economic impact of the political difficulties with Mauritania and The Gambia.

The ability of local industrial firms to adjust rapidly to competitive pressures, legitimate as well as illegitimate, was further weakened by the failure of donors and the Government of Senegal to implement a full range of complementary reforms (*mésures d'accompagnement*)—for example, providing easily accessible credit for refinancing and modernization, establishing labor legislation to streamline work forces, lowering costs for production inputs, and streamlining Government administrative requirements. As of January 1990, with the exception of minor administrative adjustments, none of the complementary measures had been implemented.

Finally, the commitment of the Government of Senegal to creating effective stimuli for expanding privately managed productive capacity was weakened by an unfavorable political situation and the conflicting agendas of donors participating in industrial sector reforms. Hotly contested presidential and legislative elections in February 1988 prevented the Government from negotiating critical labor legislation reforms with Senegal's aggressive labor unions. In addition, the urgent concerns of the International Monetary Fund (IMF) for reversing declining revenues resulted in the Senegalese Government increasing tariff rates in August 1989 (contrary to AEPRP-I agreements).

Similarly the politics of the French Government were ambiguous, marked by concerns for easing the shock of international competition to French-owned enterprises and for easing the desperate fiscal situation of the Government of Senegal. Both A.I.D. and the World Bank maintained support for industrial sector reforms, but neither was outspoken in dealing with reform backsliding or with the failure of donors and the Government of Senegal to implement complementary reforms.

Despite the weight of these external factors and the relatively short time in which the reforms had become operational, the evaluation revealed that the A.I.D.-supported reforms were already showing signs of desired effects. Some near-term impacts and adjustments were beginning to occur, particularly with regard to promoting private sector competitiveness and reversing the decline in Government revenues; these changes, albeit nascent, have the potential for producing the economic impacts envisioned in the reform programs. Some industrial firms visited by the evaluation team have already demonstrated a capacity to adjust to the conditions of world market competition. Implementation of complementary reforms should accelerate this process. Employers in the formal sector uniformly praised the quality of Senegalese labor, particularly at the technical and supervisory level.

One of the least understood phenomena of the adjustment process has been the impact of the reforms on the informal sector. A.I.D. has been the leader among donors in its efforts to monitor these impacts. Analyses of the most recent data from two USAID Mission-financed surveys in Dakar and Kaolack demonstrate that commercial and productive activity in the informal sector has significantly increased over the past 3 years. Increased commercial activity, linked to the ready availability of cheap consumer goods, has produced increased owner-operated businesses and participation of women in the labor force. Cheaper inputs, linked to tariff reforms, appear to have encouraged increases in investments in informal sector enterprises. Cheap imports have also provided a windfall to low-income Senegalese in both rural and urban areas, but at a potential social and economic cost.

While it is probable that Government of Senegal revenues will remain stagnant or will even decrease in the next 2 years, the impact of the A.I.D.-designed income tax reforms, authorized in January 1990, should produce increasing revenues starting in 1992. Automation of customs processing, the on-line tie-in to the Tax Service, and increased automation within the Tax Service should contribute to widening the tax base and increasing revenues. In the medium term, therefore, reforms supported under AEPRP-I have the potential for producing the adjustment and revenue-generating impacts envisioned in the Program Agreement.

Key lessons learned from AEPRP-I include the importance of (1) negotiating and monitoring donor commitment to a set of reforms critically linked to the success of A.I.D.-sponsored reforms, (2) establishing effective communication with the groups centrally affected by the reforms and envisioning appropriate mid-course adjustments, (3) being sensitive to political events that can hinder the impact of the desired adjustments, and (4) coordinating competing donor agendas and being aware of the potential impact of those agendas on the course of implementing policy reforms.

ANNEX C

INDUSTRIAL SURVEY FINDINGS

(From: Senegal's Industrial Sector Under the New Industrial Policy (NIP), by Eckhard Siggel, October 1991, pp. 29-31)

1. THE OUTCOME OF NIP

(a) From the preceding analysis and discussion we conclude that the NIP has had, until now, more negative than positive effects on the industrial sector. Although supporting quantitative evidence is not yet at hand, the aggregate losses in production and employment appear to have outnumbered the gains in newly created activities. The new opportunities appear to be scarce and difficult to demonstrate. Even after nearly five years of application of the new regime, the positive benefits are much harder to find than the costs in terms of lost income and employment.

(b) The negative effects are hardly attributable to the objectives and originally planned policy changes per se. Those planned changes were relatively modest and would have provided sufficient potential protection for industries. The tariff reform by itself would have led to a more uniform structure of protection, even after the 1989 and 1990 reversals. But additional factors have contributed to failure in achieving this goal.

(c) The main reasons for the lack of success of the program are:

- (i) inappropriate timing and sequencing of the measures,
- (ii) incomplete implementation, and
- (iii) inconsistency in application.

(d) A major flaw in the reform implementation was, and is, the declining power of the main policy tool, the tariff (defined here as the sum of customs and fiscal duties), due to the growing inefficiency of customs administration. It can be described as case of bad timing, since the Government did plan a reform of the customs administration. The reform was implemented only in 1989, however -- two years after the first reductions of trade barriers. In addition, the reform of customs administration has not been operational until recently. It can be argued that the NIP followed the wrong sequence. If lowered tariffs are to provide all of the planned protection, replacing various forms of nontariff barriers, then the customs administration itself has to be rendered efficient prior to the liberalization. If the sequence is reversed, as in Senegal's case, it becomes much more difficult to implement administrative reform, and during this period industries suffer from a tide of smuggled imports.

(e) Inappropriate timing has also plagued the program with regard to the accompanying measures. The change of existing labor laws as well as the adjustment of "technical" cost of factors have been delayed to such an extent that the private sector lost much of its good will and confidence in the reforms. The line of credit, APEX, which was destined to finance the restructuring of the industrial sector, was also made available much later than planned, and proved inadequate for the task it was to accomplish.

(f) Incomplete implementation applies to several actions, the administrative reform of customs, the full harmonization of tariff protection (codes de precision and mercuriales) and several of the accompanying measures.

(g) Inconsistency in application refers to the maintenance of privileges for some firms (due to conventions) increasing the distortions vis-à-vis the firms whose protection was lowered.

(h) On the positive side, we have found some limited evidence of increased efficiency in several industries. Neither aggregate data nor our data base are complete enough to prove the point. Only interviews with representatives of firms have provided some evidence of rationalization, mainly be reducing employment.

(i) it could also be argued, based on various interviews, that the informal sector has absorbed most of the workers that were released by declining industries. We have no systematic evidence of this phenomenon, although, at least in the commercial sector, it is quite evident to the casual observer. But even if statistics were to show this to be the case, it would not mean that manufacturing, rather than only commercial activity, is expanding into the small-scale sector. In addition, it should be recognized that the proliferation of informal sector production is not a valid replacement of manufacturing activities in terms of technological and managerial learning that undeniably goes with large-firm industrialization.

(j) It would be interesting to examine whether the other goals of NIP have been accomplished or approached, namely the disengagement of the State, the higher value-added goal or the expansion of industrial fabric into small and medium-sized enterprise. Another set of data would be needed for these tasks.

ANNEX D

ANNOTATED BIBLIOGRAPHY

<u>Studies</u>

The following studies were completed by short-term consultants and USAID/Dakar staff under the African Economic Policy Reform Program (AEPRP I Program):

(1) <u>A preliminary Report Of A Brief Survey Of Senegal's Direct Taxes,</u> Olivier Oldman, June 30, 1986: This preliminary report examined direct tax modernization policy for Senegal and provided the perspective of Americans on the process of changing the direct tax system to fit medium and longer term changes in Senegal's economy and society.

(2) <u>Senegal's Tax System And Tax Reform</u>, USAID/Senegal (Dakar) Program Office, March 10, 1987 and October 22, 1987: The two reports mentioned the six broad groups of the Senegalese tax system and showed a detailed breakdown of tax receipts and the weaknesses of Senegal's tax system.

(3) <u>Final Report: Monitoring/Evaluation Plan Implementation AEPRP GRANT - USAID/Senegal</u>, Tvt Associates, July 27, 1987: The monitoring and evaluation system developed by TvT concentrated on the design of a micro-economic monitoring system for industrial production in Senegal, which furnished current data on inputs and outputs of a group of nineteen products comprising a major part of the formal Senegalese production sector. The final report was under Delivery Order No.3, Contract Number PDC-0085-I-00-6108-00.

(4) <u>Impôts Directs Du Code Des Impôts Du Sénégal, Les Réformes Possibles Et Les Problèmes Y Afférents,</u> H. David Rosenbloom, 28, Décembre 1987: The report contained recommendations for simplification and improvement of the existing tax legislation and specific guidance on the future activities of the GOS Tax Department's Legislative Drafting Group on Direct Tax Reform.

(5) <u>Audit of the Senegal African Economic Policy Reform Program; Project No. 685-0291; Audit Report No. 7-685-88-15,</u> USAID/RIG, Dakar, July 19, 1988: The Audit objectives were to assess the adequacy of the USAID/Senegal system for measuring program effectiveness, to determine the extent to which the program had achieved desired results, and to identify factors inhibiting performance.

(6) <u>Preliminary Analysis Of The Impacts Of Senegal's Industrial Policy On Selected Branches Of Industry</u>, Assitan Thioune, Program Office, USAID/Dakar, October 18, 1988 and May 22, 1989: These two reports are only a partial analysis of the effects of the NIP on certain branches of industry.

(7) Tax Reform In Senegal 1986-1990: The Impact of the African Economic Policy Reform Program on the Implementation of Senegal's New Industrial Policy, Jim Lowenthal, Gerard Chambas, John Lewis, James T. Smith, January 1990: The report reviewed the impacts of the reforms, the methods and analysis used to distinguish effects from exogenous factors, and the lessons learned in promoting industrial restructuring through tariff and tax reform in Senegal. This report was reissued in September, 1990 as A.I.D. Impact Evaluation Report No.77, The A.I.D. Economic Policy Reform Program in Senegal.

(8) Trip Report - Dakar, Senegal USAID Evaluation System Of the Effects Of the NIP in Senegal, Jean-Claude Berthelemy, Tvt Associates, April 10-20, 1990: The purpose of this trip concerned the management of the industrial data base and preparation of the quarterly reports.

(9) Trip Report - AEPRP1 Monitoring System, Joy, E. Hecht, Tvt Associates, August 27, 1990 and September 7, 1990: The reports updated and analyzed statistical data and provided technical assistance to the Statistics Department of the GOS Ministry of Economy and Finance in computerizing and analyzing the data generated by the Statistics Department's industry surveys.

(10) USAID Evaluation System Of the Effects Of the NIP in Senegal, Jean-Claude Berthelemy, Tvt Associates, August 29-September 7, 1990, and September 12, 1990: The purpose of these reports were to complete the industry interviews for the food industry and the chemical industry sector and to provide reports on these interviews. These services were under Contract Number AFR-0291-C-00-0009-00 AEPRP1 Monitoring System.

(11) Sectoral Report: Analysis of the Impacts of Senegal's Industrial Policy on Textile and Shoes Industries, Assitan Thioune, USAID/Senegal, Program Office, June 14, 1990 and November 16, 1990: Under AEPRP-1 (685-0291/685-K-605A) Monitoring Component.

June 14, 1990: The analysis consisted of a comparison of indices for output, sales, exports, and prices for enterprises grouped into 19 branches for both pre-NIP and post-NIP periods.

November 16, 1990: The Senegal industrial restructuring program, commonly known as the New Industrial Policy (NIP) was initiated in 1986 as part of Senegal's medium and long term Structural Adjustment Program. The document analyzed the four global objectives under the New Industrial Policy.

(12) Analysis of the Impacts of Senegal's Industrial Policy on the Food Processing Sector, Assitan Thioune, USAID/Senegal, Program Office, December 19, 1990 AEPRP-1 (685-0291/685-K-605A) Monitoring Component: The analysis concerned domestically consumed products (wheat flour, sugar, tomato paste and biscuits) and exporting industries such as SONACOS which exports crude peanut oil and other peanut products. The analysis also focused on fish processing, canning and freezing and on processing of powdered milk.

(13) Review Of Tax Training Assistance Project Proposals For Additional Training Assistance Directorate General Of Lands And Taxes, Republic of Senegal, Supplemental Reports, Richard Leonard, April 26, 1991 and May 15, 1991.

April 26, 1991: The purpose of this supplemental report was to provide detailed technical assistance proposals in Audit Techniques/Training area and Land Record Preservation/Training, Management Development and Training, Taxpayers Service and Education areas.

May 15, 1991: The purpose of this document was to establish a proposed project implementation plan for a two-year, on-site technical assistance program focusing primarily on the control and audit functions of the Senegalese Tax Department.

(14) Subsector Report: The Industrial Subsectors Of Chemicals And Intermediate Products In Senegal Under The New Industrial Policy (NIP), Eckhard Siggel, Ph.D., October 1991, Contract Number AFR-0291-C-00-0009-00. The basic objective, as in the main report, was to investigate the impact of the NIP on the levels of protection and activity in several industries of this subsector. This report supplements the broader report, Senegal's Industrial Sector under the New Industrial Policy.

(15) Final Report of Senegal's Industrial Sector Under the New Industrial Policy (NIP), Eckhard Siggel, Ph.D., October 1991, Contract Number AFR-0291-C-00-0009-00: Senegal's New Industrial Policy (NIP) was initiated in 1986. It was part of the country's Medium-and long-Term Adjustment Programme, essentially a trade policy reform combined with various measures destined to facilitate the transition and to help domestic industries in becoming more competitive with imports and in external markets. This report provides a synthesis of work done under the Industrial Sector Monitoring and Evaluation component of AEPRP-1.

P:\DAKARPUB\DOCS\ANNOTABI

AEPRP-I (685-0291) PACR

Clearances: PRM/AS:CCOwey 4/29/94
OFM:WMcKeel 5/10/94
PRM:MAKane 5/16/94
PRM:JvdVeen 5/31/94

P\PRMPUB\DOCS\ANNOTABI

BEST AVAILABLE DOCUMENT