

# APPENDIX **2**

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## ADB EXPERIENCE ON THE MACROECONOMIC CONTEXT SECTION OF PROGRAM LOAN REPORTS

This appendix reviews the discussions on the macroeconomic context section that emerge from an examination of the IO core program loan reports. Primarily, the quality of assessment of the macroeconomic context in the program loan reports is uneven, and is sometimes compounded by the lack of identification of variables that may result in critical feedback effects.

### **A. Key Points on How to Improve the Discussion of the Macroeconomic Context**

**I. Presentation of the Macroeconomic Context.** There is variability among the program loan reports in terms of the data presented, economic projections, macroeconomic assessment, and the relevance of the macroeconomic context. Inconsistency arises due to lack of a clear application of the macroeconomic assessment in developing the reform program, as well as uncertainty on how to effectively and efficiently undertake such assessment. The ultimate goal should be to identify the critical macro-meso-micro linkages that will affect the costs, benefits, and risks to the reform program. Recommended coverage should include: (i) a review of economic growth performance, (ii) assessment of macroeconomic management performance, (iii) discussion of key structural policies, (iv) outlook for economic performance over the relevant program period, and (v) a summary of the macroeconomic linkages and assumptions to be included in the macroeconomic framework.

**2. Data Presented.** A discussion of the macroeconomic context should include a minimum set of key indicators. There is inconsistency across the program loan reports in terms of data presented even though ADB's economic reports and country strategy and program documents provide an accessible and standardized set of economic indicators. However, additional details may need to be provided by the analyst. Tables presented in the program loan reports should include precise definitions of variables reported. It is also important to consider the quality of the data being presented and their appropriateness to the analysis. For example, aggregate investment data for many least-developed countries is often imprecise. Sector decompositions of investment should be interpreted with care in countries with high levels of public sector or SOE investment, or programs that would channel investments to favored sectors.

**3. Economic Projections.** The program loan reports usually include a section on medium-term prospects and projections. However, these sections often do not distinguish between ADB staff projections and government macroeconomic targets and development goals. ADB projections for the next 2 years for key indicators are readily available in the annual *Asian Development Outlook* and should be used as appropriate. However, because ADB does not generally provide long-term projections, it is acceptable to use government targets and development goals where the program horizon makes

long-term projections necessary. In cases like these, the program loan report should clearly identify government targets and projections and critically assess the reasonableness of the data.

**4. Macroeconomic Assessment.** The program loan reports generally do not exhibit a consistent and systematic approach to progressive discussions of past trends, current performance, and prospects. Moreover, there is a tendency to support broad conclusions with limited information. This can be avoided by adhering to a standard format (in which discussion of prospects is kept separate), and by having a thorough familiarity with macroeconomics and the unique characteristics of a particular economy. Where judgments are to be made regarding recent economic performance and reform programs, a number of criteria should be used, including, as appropriate, trends in growth of output and incomes, employment, income inequality, and poverty.

**5. Relevance of the Macroeconomic Context.** While the description of the macroeconomic context is adequate in some cases, its relevance and linkage to the subsequent sector and program description are, often, unclear. The description can be pro forma and superfluous to the program loan report, and may miss key macroeconomic influences on the sector and the subsequent program. To avoid the tendency toward a mechanical review, a final section of the macroeconomic context section of the RRP should provide an overall

assessment of those macroeconomic factors that are most critical to policy operations. These should form the basis of the macroeconomic framework.

## **B. Basic Considerations for Improving Macroeconomic Assessment for Policy Operations**

As discussed in Chapter 2, a sufficient understanding of the macroeconomic environment is needed to gain insights into the context and possible feedback effects of sector reform measures. The basic minimum for the assessment, concerning the review of key macroeconomic indicators, usually presented in a series of 5 or more years plus projections as appropriate, provides a minimal snapshot of the macroeconomic environment. In the ADB context, analysts should be careful in properly defining and accurately reporting this data set (2-year projections for this standard set). The data set may need to be expanded to provide a more complete picture of the macroeconomic context, depending on the specifics of the policy reform exercise and after these key indicators have been used for preliminary perusal. (Key macroeconomic indicators for Cambodia are provided in Table A2.1 as an illustration.)

Several other points are emphasized. First, it is not necessary for the analyst to undertake a detailed assessment of the macroeconomic performance of the economy. A country economist at ADB is an important resource person for a policy operation, whose expertise should be used. Second, the analysts should be

TABLE A2.1: Key Economic Indicators

Item	1997	1998	1999	2000	2001 <sup>a</sup>
<b>Output Growth</b>					
GDP per capita (\$, current)	281	247	264	261	259
GDP Growth (percent, in constant prices)	4.3	2.1	6.9	7.7	6.3
Agriculture	5.5	3.0	0.0	(0.3)	3.9
Industry	21.3	7.3	13.2	34.6	15.5
Services	(2.6)	0.7	7.1	5.8	2.9
<b>Savings and Investment</b> (current and market prices)					
	( % o f G D P )				
Gross Domestic Investment (% of GDP)	14.3	11.3	15.9	13.5	17.9
Gross National Savings (% of GDP)	9.0	9.5	11.8	6.9	9.6
<b>Money and Inflation</b> (annual % change)					
Consumer Price Index	9.1	12.6	0.0	0.5	(0.5)
Money Supply (M2)	16.6	15.7	17.3	26.9	20.4
<b>Government Finance</b> ( % o f G D P )					
Revenue and Grants	9.0	8.3	10.6	11.0	11.4
Expenditure and On-lending	13.0	13.8	14.5	16.3	17.5
Overall Fiscal Surplus/(Deficit)	(4.0)	(5.5)	(3.9)	(5.3)	(6.0)
<b>Balance of Payments</b>					
Merchandise Trade Balance (% of GDP)	(7.1)	(5.8)	(8.3)	(7.8)	(6.6)
Current Account Balance (% of GDP) <sup>b</sup>	(8.2)	(6.9)	(7.8)	(7.6)	(6.4)
Merchandise Export (\$) Growth (annual % change) <sup>c</sup>	81.0	13.0	17.9	53.2	9.9
Merchandise Import (\$) Growth (annual % change) <sup>c</sup>	5.8	1.6	27.0	37.1	5.2
<b>External Payments Indicators</b>					
Gross Official Reserves (including gold, \$ million)	262	390	422	485	548
(in weeks of current year's imports of goods)	10.6	16.2	16.1	14.2	15.3
External Debt Service (% of export of goods and services)	1.2	2.1	1.6	4.0	4.0
Total External Debt (% of GDP)	62.9	71.3	67.4	65.5	64.2
<b>Memorandum Items:</b>					
GDP (current prices, KR billion)	9,778	11,364	12,587	12,932	13,365
Exchange Rate (KR/\$, average)	2,991	3,774	3,814	3,859	3,924
Population (million)	11.6	12.2	12.5	12.8	13.1

( ) Negative.

GDP = gross domestic product.

<sup>a</sup> Provisional.<sup>b</sup> Excluding official transfers.<sup>c</sup> Some imports are reexported to neighboring countries, e.g., Viet Nam.

Data sources: Ministry of Economy and Finance, National Institute of Statistics, National Bank of Cambodia, International Monetary Fund, and ADB staff estimates.

Source: Cambodia Country Strategy and Program Update (2003–2005).

cautious about importing into the policy framework the analysis conducted by another institution. For example, the IMF reports, which are produced specifically for IMF operations, may not cover aspects of the economy crucial to the policy, may contain targets for key indicators rather than projections, or may base some projections on assumptions that are not

made explicit. Thus, externally produced reports should be treated only as sources of information. Third, the analysts should focus on answering key questions about the macroeconomic context in the assessment, and not on a pro forma review. Fourth, the depth of the discussion in each section of the analysis will depend on its importance to the analysis of the reform measures.