

**FOR
AGENDA**

EBD/04/109

October 1, 2004

To: Members of the Executive Board

From: The Secretary

Subject: **Republic of Madagascar—Poverty Reduction Strategy Paper Annual Progress Report—Joint Staff Assessment**

Attached for consideration by the Executive Directors is the assessment, prepared jointly by the staffs of the Fund and the International Development Association, of the poverty reduction strategy paper annual progress report for the Republic of Madagascar (EBD/04/108, Volumes I and II, 10/1/04). These papers, together with the paper on the fifth review under the Poverty Reduction and Growth Facility for the Republic of Madagascar and its requests for a waiver of nonobservance of performance criteria and modification of performance criteria (EBS/04/140, 9/30/04), are tentatively scheduled for discussion on **Monday, October 18, 2004**. At the time of circulation of this paper to the Board, the Secretary's Department has not received a communication from the authorities of the Republic of Madagascar indicating whether or not they consent to the Fund's publication of this paper; such communication may be received after the authorities have had an opportunity to read the paper.

Questions may be referred to Mr. Fayolle (ext. 35976) and Mr. Nassar (ext. 38665) in AFR.

Unless the Documents Section (ext. 36760) is otherwise notified, the document will be transmitted, in accordance with the procedures approved by the Executive Board and with the appropriate deletions, to the WTO Secretariat on Tuesday, October 12, 2004; and to the African Development Bank, the Common Market for Eastern and Southern Africa, the European Commission, the Food and Agriculture Organization, and the United Nations Development Programme, following its consideration by the Executive Board.

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THE INTERNATIONAL DEVELOPMENT ASSOCIATION AND
THE INTERNATIONAL MONETARY FUND

REPUBLIC OF MADAGASCAR

**Poverty Reduction Strategy Paper—Annual Progress Report
Joint Staff Assessment**

Prepared by the Staffs of the International Development Association and
the International Monetary Fund¹

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I. OVERVIEW

1. **The First Progress Report of the Government of Madagascar on the implementation of the poverty reduction strategy covers the period July 2003 to June 2004.** This Progress Report highlights the results achieved, lessons learnt and challenges faced in implementing the poverty reduction strategy paper (PRSP), which was prepared by the Government in July 2003 and was discussed by the Boards of the IMF and World Bank in November 2003.
2. **Following a strong noninflationary growth performance in 2003, macroeconomic developments in 2004 have been affected by adverse exogenous shocks.** In January and March 2004, Madagascar was hit by two cyclones, which rendered thousands homeless, caused widespread damage to infrastructure and significant agricultural output loss. Since the beginning of the year, the Malagasy currency depreciated by about 40 percent against the euro, owing notably to a significant deterioration of the trade account. The exchange rate stabilized in July – August 2004, but inflationary pressures have significantly increased. In order to limit second-round effects (for example, wage increases, and price increases in services) of the supply side and exchange rate shocks on inflation, the Government has begun to implement a broad-based policy package, including monetary policy tightening and fiscal measures.
3. **Madagascar is making good progress in implementing its poverty reduction strategy, which is delivering results.** Primary net enrolment rates have increased from around 70 percent in 2002 to 84 percent in 2003/04. The roads program has been successful and rehabilitated about 1850 kms of roads, a three-fold increase over 2001.

¹ This Staff Assessment was prepared jointly with the African Development Bank, the European Commission, and the United Nations Development Program.

After the sharp (estimated) increase in the poverty rate during the 2002 crisis, poverty declined significantly in 2003, though remaining above its 2001 level of 69.6 percent.

4. **The Progress Report confirms several major strengths of the PRSP.**

Ownership remains high, and the process continues to be participatory and open. An intermediate Progress Report covering the first six months of implementation was discussed extensively, during a series of thematic and regional workshops between March and May 2004, involving a wide range of stakeholders (including the private sector, NGOs, and Government). The purpose of these workshops was to receive feedback on the impact of the policy measures taken to date. Donors also provided comments on the report. The poverty diagnostics are comprehensive and provide a wide range of information on the evolution of poverty. Donor assistance is being coordinated in support of the implementation of the PRSP.

5. **The Progress Report addresses some of the weaknesses identified in the Joint Staff Assessment of the PRSP.**

First, progress had been made in prioritizing public actions in important areas such as public expenditure management, justice and anti-corruption. Second, for each sector, intermediate monitoring indicators that allow for progress to be monitored on a more regular basis are specified, and the indicators and targets in education and health have been jointly agreed between the Government and the development partners. Third, the strategies in agriculture, health, and nutrition being implemented are much more informed by why public service delivery has failed in the past.

6. **But weaknesses remain, and further progress is needed in prioritizing and costing the strategy.**

The PRSP actions remain ambitious and will test the implementation capacity of the Government. The Government will need to continue to focus on capacity building to ensure successful implementation. First, the staffs recommend that the budget for 2005, both the allocation across and within sectors, be closely aligned to the strategic priorities of the PRSP, and efforts be made to improve the costing of the PRSP. Second, the staffs recommend that the Government prepare sector strategies, including costing, in key sectors such as health and social protection. Third, from a presentational point of view, the Progress Report presents a large amount of information, which often makes it difficult to understand the strategic directions. The staffs recommend that the executive summary of the next Progress Report provides an overall assessment of the poverty reduction strategy, including prioritized actions for the upcoming year and the risks. Fourth, as noted in the previous JSA, the report lacks a discussion of risks and risk mitigation measures that could affect implementation.

II. IMPLEMENTATION OF THE STRATEGY AND PROSPECTS FOR 2005

A. Poverty Reduction

7. **The staffs welcome the range of data presented on poverty – including a survey of perceptions conducted by INSTAT in 2004, and simulations of the poverty impact of the pattern of growth.** The poverty analysis is based on the 2001 household survey (Enquête Prioritaire auprès des Ménages, EPM), and presents the trends and

determinants of poverty (lack of education and remoteness are important factors). Based on simulations, poverty is estimated to have increased sharply from 69.6 percent in 2001 to around 80 percent during the 2002 crisis, before declining to 73.6 percent in 2003, and showing a slight increase to 75.4 percent in May 2004. Urban areas benefited more from the resumption of growth than rural areas. As noted before, progress is also evident in the education sector (increased enrollment rates, primary school completion rates) and in health (improved immunization rates, child mortality). These results are also confirmed by the survey of perceptions of the evolution of living standards and the implementation of the PRSP. Over six out of ten households note the improvement in education, and health, national roads and safety also score high. The staffs recommend that the next Progress Report present the results of the 2004 household survey (including an updated poverty analysis and employment study), which will be completed by the end of year.

B. Macroeconomic Policies

8. **Since the full PRSP was prepared in July 2003, Madagascar's macroeconomic performance under the PRGF arrangement was mixed.** In 2003, real GDP growth exceeded the target, and inflation was much lower than expected. However, fiscal performance was weaker than programmed, due mainly to tax and tariff exemptions that took effect in September 2003 and continuing weaknesses in customs administration.

9. **Program implementation in 2004 has been significantly impacted by adverse exogenous shocks and by some policy slippages.** The Malagasy Franc (FMG) depreciated by about 40 percent against the euro since the beginning of 2004. Several factors contributed to this development, including (i) strong imports as a result of higher petroleum prices, increased Government capital expenditures to finance priority sectors, and an acceleration of private imports linked to the tariff and tax exemptions granted in 2003; and (ii) weaker exports of shellfish and vanilla, owing to the impact of the cyclones. The exchange rate has stabilized over the summer. Real GDP is estimated to grow by about 5 percent in 2004, compared with 6 percent expected. Structural reforms proceeded more slowly than planned, but progress was made in the anticorruption drive, public expenditure management, reform of the tax and customs departments, reform of the interbank foreign exchange trading system, and modernization of land ownership legislation.

10. **Inflation accelerated sharply since the beginning of the year, reflecting the impact of two cyclones on agricultural output, higher international rice and petroleum prices, and partial pass-through of the depreciation of the currency.** Inflation rose to over 17 percent (on a year-on-year basis) in July 2004. Excluding rice and petroleum, inflation was 6 percent. The rise in inflation calls for prudent macroeconomic policies, aimed at achieving the medium-term macroeconomic objectives of the PRSP and limiting the second-round inflation effects of the supply side and exchange rate shocks. The authorities have begun to implement a supporting broad-based policy package, including monetary tightening measures and fiscal measures to increase revenue (including rescinding of VAT exemptions on consumer goods) and contain expenditures. A social safety net program for the vulnerable was announced.

Even though the progress report discussed the risks to macroeconomic stability and measures already taken, staffs note that the authorities must remain committed to limiting the second-round effects of the supply-side shocks on inflation.

11. **While the macroeconomic framework set out in the PRSP is considered sound, recent developments illustrate important risks to the attainment of the desired macroeconomic objectives.** In particular, controlling inflation is vital to the success of the poverty reduction strategy, because the poorest people are also those most vulnerable to inflation. Meanwhile the staffs note that Madagascar must strengthen its supply response (including through diversification of the economy), in order to take advantage of the competitiveness gained in recent months to achieve the PRSP objectives.

C. Governance and Public Sector Management

12. **The Government has made progress in implementing its public expenditure management reform plan, and sustaining this momentum is critical.** The implementation of the 2004 Priority Action Plan for public finance reform is well under way. Based on this plan, the Government is strengthening the budget preparation process (e.g. by aligning the budget closer to PRSP-priorities) as well as budget execution (e.g. by streamlining the expenditure management process) and introducing a medium term perspective into the budget (through the introduction of program budgeting). The 2004 budget saw significant increases in the allocation to key PRSP priorities (such as education and transport) and is very much poverty reduction oriented. Other key reforms include the implementation of the recommendations of the independent audit of the Treasury, the approval of the new Procurement Code by Parliament, and strengthened internal and external budget controls. The key challenge over the next twelve months will be to build on the momentum created by these initial reforms. The Priority Action Plan for 2005 should focus on strengthening the Treasury, public procurement, and public financial management capacity in other PRSP priority ministries (education, health, transport). In addition, the staffs recommend that the Government improve its communication on the implementation of the Priority Action Plan.

13. **The Government has made significant progress in strengthening the regulatory and institutional framework for anti-corruption.** An anti-corruption strategy has been developed, and legislation strengthening existing preventive and punitive instruments has been submitted to Parliament. The independent Anti-Corruption Bureau is expected to be established and staffed in September 2004. Government is also committed to conducting independent audits of (randomly selected) investment projects and of specific public services. The staffs recommend that, in the coming year, the Government focus on decisively implementing anti-corruption reforms, in particular by addressing corruption in Government services in which corruption is perceived to be significant (including police, medical centers, land titling agencies, customs, and lower courts).

14. **However, progress has been slower in customs and the judiciary.** The PRSP Progress Report rightly notes the importance of the joint private/public sector committee

established by the Government to oversee the implementation of the tax and customs reforms. However, customs reforms have been piecemeal and have not yet had the desired results. Moving forward, the staffs recommend that the Government closely monitor the reform program for customs through a time-bound action plan. Staffs also propose that regular anti-corruption surveys be conducted. As far as the judiciary is concerned, the reduction of the backlog of cases at the lower courts has been slow. The introduction of service standards for the magistrates and other service personnel has been delayed by several months. The activities aimed at improving the operational efficiency of the commercial sections of the lower courts need to be strengthened so as to yield the intended results. The staffs recommend that in the coming year Government address these bottlenecks on the basis of a transparent and monitorable action plan.

D. Structural Policies for Growth and Investment

15. As noted in the previous JSA, the staffs support the three guiding principles underlying the policies aimed at stimulating growth and investment—(i) major investment in the public transport infrastructure to integrate farmers into the market; (ii) commitment to public-private partnerships in the management of key public enterprises; and (iii) improving the investment climate.

16. **The ambitious transport sector program has been successful in rehabilitating the road network. However, structural reforms have been slow and need to be accelerated.** The physical progress of the sector program is quite impressive with about 1,850 km of roads rehabilitated in 2003, a three-fold increase over the levels in 2001/2002. To sustain these achievements, sector reform, including the creation of effective regulatory agencies, the concessioning of the operation of transport facilities, with the sector ministry focusing on oversight, coordination and planning, needs to be accelerated and deepened. The Port, Maritime, and River Transport Authority (APMF) has been established and is functioning. The ACM (Civil Aviation Authority) is awaiting further restructuring, and the creation of the ATT (Agency for Terrestrial Transport) and the AR (Road Authority) has been delayed and is now expected by the end of 2004.

17. **The Government has made progress on public enterprise reform.** The privatization of the telecommunications company, TELMA, was completed in June 2004. The private company that will manage the sugar company, SIRAMA, was selected in June 2004, and the company that will manage the energy company, JIRAMA, is expected to be selected by October 2004. The contract for the privatization of the cotton company, HASYMA, is expected to be awarded by end-September 2004.

18. **In the past year, the Government has taken measures to improve the investment climate.** This includes a one-stop shop for facilitating enterprise creation which became operational in October 2003 in the capital and Toamasina. The one-stop shop has reduced considerably to less than a week the time needed to set up a firm. Legislation allowing foreigners to own land was also passed. The Bank is supporting an Investment Climate Survey and a Financial Sector Assessment Program, jointly with the IMF, to be undertaken in 2005. The staffs recommend that the next Progress Report reflect the findings of these studies.

E. Trade

19. **Given the small size of the domestic market, the Government considers trade and expansion of exports as a critical condition for private sector development, sustained high growth, and poverty alleviation.** Therefore, mainstreaming trade policies and improving competitiveness have been an important policy objective of the Government to integrate the Malagasy economy into global markets. To achieve this objective, the Government accelerated implementation of the Integrated Framework (IF) program and the recommendations of the Diagnostic Trade Integration Study (DTIS). In particular, the Government (i) set up a Steering Committee representing all stakeholders to oversee the implementation of the trade reform program, (ii) simplified the tariff structure and lowered the weighted average tariff rate from 18 to 14 percent, (iii) initiated reforms to accelerate customs clearance; (iv) simplified regulations on subcontracting of EPZ operations to small local companies, (v) streamlined approval of investment projects through the establishment of a one-stop counter, and (vi) prepared a comprehensive technical assistance program to improve capacity in the Government and the private sector to formulate and implement trade policies and negotiate trade agreements. The Government is also actively participating with other 15 COMESA members in negotiations for an Economic Partnership Agreement (EPA) with the EU, and making preparations to join SADC.

20. Moving forward, Madagascar will need to continue to simplify its tariff structure; improve export services; analyze the costs and benefits of joining SADC and develop a negotiating strategy to maximize the benefits of membership to Madagascar; assess the impact of the end of the Multi-Fibre Agreement and take necessary measures to adjust to the new market conditions in the textile sector; and implement its capacity building plan, with donor support. The staffs recommend that the next Progress Report include a clear articulation of the Government's external trade priorities.

F. Rural Development and Environment

21. **The environment and rural development agenda of the PRSP remains of critical importance to reduce poverty in Madagascar, as close to 80 percent of the poor live in rural areas.** Staffs note with satisfaction the favorable agricultural growth in 2003 (3.5 percent), following the resumption of transportation links between production regions and urban markets, the rehabilitation of irrigation infrastructure and the increase in fertilizer use. This supports emerging evidence that the adopted strategy for rural development and environment under the PRSP is in essence sound.

22. **First, the staffs see important progress in the rural and environment sector.** Following feedback provided under the previous JSA, staffs appreciate the efforts that have been undertaken to better understand why past policies and investments in the sector have failed as the basis for better prioritization of activities under the strategy. In this context, a number of achievements stand out, including: (i) elaboration of Master Plans for the agriculture, livestock and fisheries sub-sectors; (ii) up-date of the Policy Letter for Rural Development; and (iii) adoption of a Policy Letter of Environmental Policy. The staffs feel that these policy statements could be better integrated into the PRSP progress

report. Staffs recommend that the budget for 2005 for the agriculture and environment ministries reflect the strategic priorities outlined in the policy documents. In addition, there is a need to better understand these linkages in quantitative terms by scaling-up of modeling exercises that link sector investments to agriculture growth that have recently been launched by the Policy Unit for Rural Development.

23. **Second, the staffs urge that the implementation of ongoing institutional reforms be accelerated.** Staffs encourage the specification of measures to move from the design into the implementation phase in the following areas: (i) setting-up of the new institutional structure of the Ministry of Agriculture, Livestock and Fisheries aimed at ensuring greater focus on core functions and bringing it closer to the field with 70 percent of its operational budget spent at the regional level; (ii) establishing the new agency for forestry management aimed at improving governance in the forestry sector by separating policy-making and regulatory functions from operational responsibilities; (iii) making the *Fonds d'Entretien des Réseaux Hydro-Agricoles* (FERHA) for irrigation infrastructure fully operational, including ensuring that it is adequately financed; and (iv) deepening efforts to coordinate public investments, particularly in agriculture, roads, forestry and protected areas, for improved synergy.

24. **Third, while the progress in promoting environmentally sustainable natural resource management is encouraging and consistent with the established results framework, there is a need for accompanying measures to provide adequate incentives and improve the institutional arrangements.** These include: (i) enhancing compliance of public sector investments with existing MECIE (*Mise En Compatibilité des Investissements avec l'Environnement*) legislation by requiring sector ministries to incorporate adequate budget provisions for environmental impact assessments in their investment programs; (ii) ensuring more sustainable financing of Madagascar's protected areas system by establishing a transfer mechanism that would more directly link tourist sector revenues (e.g. visa payments) and operating and maintenance costs of protected areas; (iii) improving management of coastal and marine resources by recognizing in the budget allocation process a more direct correlation between fiscal revenues generated in the sector and corresponding control and surveillance costs; and (iv) recognizing the environmental (deforestation) and health costs (indoor air pollution) of the use of charcoal consider levying a tax that reflects these costs and provides incentives for more efficient production and use of charcoal as well as the adoption of substitute fuels.

G. Education

25. **As noted in the previous JSA, the staffs agree with the outlined strategy in education and actions to meet the goals.** The Government's main priority remains the Education for All (EFA), and the Government has agreed on a key set of performance indicators to measure progress in implementing the EFA, to which all the development partners have subscribed. However, staffs are concerned about capacity in the Ministry of National Education and Training (MENRS)—especially in budget formulation, procurement, financial management and monitoring—and donors are providing technical assistance for strengthening capacity in these areas.

26. **The Malagasy education and training system is in the process of reform since mid-2002. Primary enrolments increased significantly, but system weaknesses and cost-inefficiency remain.** National consultations resulted in the national “Education For All” (EFA) plan and the Education Sector Strategy, which were also presented to the international donor community.² Implementation of the EFA program since 2002 resulted in a large increase in primary net enrolment from about 67 percent in 2001/02 to over 84 percent in 2003/04. However repetition rates are high and the primary completion rate is low (40 percent). Measures taken by the Government to improve primary education delivery over the period of 2002-2004 include: (i) elimination of schools fees for public and private primary schools, (ii) strengthening community links to schools, (iii) providing more pedagogic inputs for students and teachers, (iv) making cash payments to Community-School Associations for pedagogic improvement and assisting children from the poorest families, (v) reorganizing the management in the 111 districts (CISCOs), and (vi) improving monitoring and evaluation mechanisms.

27. **The Government is working on a strategy to improve the sector’s overall performance.** Progress in the context of the Government’s PRSP objectives will require significant gains and improvements in the following areas over the next 2-3 years: (i) rapid reform of Human Resources in education; (ii) improved management capacity and quality at the central and district levels; (iii) introducing modern pedagogic principles and improved teacher and staff training; (iv) making teacher management practices (recruitment and transfers) more efficient and transparent; (v) providing the system with the necessary inputs to meet the pedagogic and administrative goals (pedagogic materials, school books and teacher guides, computerized management systems, effective MIS); and (vi) increasing access to and absorption capacity at secondary and in higher education levels.

H. Health

28. **The Progress Report shows that the health sector is implementing many effective interventions and that sector policy has evolved appropriately in light of the lessons learned.** The preliminary Demographic and Health Survey results (2003/04) show a continuing downward trend in child and infant mortality rates, although the pace of decline is still not rapid enough for Madagascar to attain the health MDGs. The Progress Report lists an impressive number of actions organized along the main objectives outlined in the PRSP, but the Report lacks an overview of the major issues addressed. A key policy action taken during the past year is the reinstatement of cost recovery in district health centers, with special provisions to exempt the poor. However, during these initial implementation stages, difficulties remain in identifying the poor, as the indigent are reluctant (for cultural reasons) to be included in these lists; and the financing allocated for this is inadequate, especially if all the needy availed themselves of this benefit. The Progress Report now outlines the complementary institutional and policy reforms needed to improve service delivery for the poor, thereby addressing an important

² The Government presented its education and training strategy and its national EFA plan during the meeting in Paris (France) of the “Amis de Madagascar” in October 2003. The international donor community accepted the strategic plans.

shortcoming in the PRSP that was noted in the previous JSA. Human resources constraints (both number and quality) continue to constitute a bottleneck for health sector performance. Technical assistance is being provided to improve the planning and budgeting capacity at the central and district level, and to develop a human resource development plan.

29. **Moving forward, the staffs recommend that the health sector strategy be updated, including estimating the costs of attaining the MDGs.** The Ministry of Health could utilize the ongoing studies in the health sector, including the newly launched Medium Term Expenditure Framework (MTEF), to elaborate the financing options. In addition, the staffs recommend that the equity funds to assist the poor at the hospital level be implemented, given the impoverishing effects of hospitalization on the poor.

I. HIV/AIDS

30. **Over the last year, Madagascar has made significant progress in strengthening the institutional and civil society response,** and partnerships to expand essential HIV/AIDS interventions, both communication and medical. A national survey shows that the prevalence rate for HIV in pregnant women was 1.1 percent in 2003. The list of activities covers most relevant domains in the fight against HIV/AIDS and should be read together with the activities reported in the health section. However, an overview of the major issues addressed is missing, making it hard to assess areas in which progress is lagging. For example, while the Information Education and Communication (IEC) network progressively ensures appropriate level of information for HIV/AIDS/Sexually Transmitted Infections, more emphasis should be put on behavioral change that shows very little progress, as evidenced by the low use of condoms with non regular sex partners reported in the last DHS. Moreover, although numerous initiatives have been taken to make medical care more accessible such as: (i) prevention of mother to child transmission (MTCT); and (ii) treatment of HIV positive cases with anti retroviral drugs in voluntary counseling and testing (VCT), the constraints should be better identified to expand coverage of these essential interventions. Finally, despite all the efforts, the level of stigmatization remains very high constituting a barrier to increase the attendance rate of MTCT and VCT centers.

J. Nutrition

31. **Madagascar is making good progress in the area of malnutrition reduction, one of the MDG targets,** which could be more clearly reflected in the Progress Report. Areas of progress include (i) the extension of the community-based nutrition interventions to 35 percent of the countries' poorest areas; (ii) the development and validation of the National Nutrition Policy coordinated by a multi-sectoral team including the Ministries of Health, Agriculture, and Planning; (iii) draft decrees for discussion for establishment of a National Nutrition Institution; and (iv) very strong donor coordination to make more efficient use of donor funding. The staffs note that the establishment of the

National Nutrition Commission and Institute to strengthen the institutional environment for nutrition is a critical next step.

K. Rural Water and Sanitation

32. **The Progress Report describes well the progress in the rural water and sanitation sector especially in the rural areas.** The institutional and legal framework for water and sanitation was strengthened significantly by passing 13 decrees related to the application of the Water Code; establishment of the national water and sanitation authority (ANDEA); and clean water and sanitation policy for urban areas. Moving forward the key priorities include the preparation of a 2005-2007 Medium Term Expenditure Framework; preparation of a water and sanitation for all strategy; and the establishment of a computerized database for improved monitoring and evaluation. As noted in the previous JSA, the relationship between the sector ministry and ANDEA still remains to be clarified.

L. Social Protection

33. **Under the safety nets and social protection sub-program, the staffs commends the Government for rapidly and efficiently addressing the disastrous consequences of cyclones Elita and Gafilo that hit the country in early 2004.** Safety nets were implemented immediately after the cyclones, relief activities, rehabilitation, and reconstruction thereafter. The requirement that all reconstruction works be cyclone-resistant should mitigate the impact of future cyclones. The staffs commend the Government for its endeavor to protect the urban and peri-urban unemployed through cash-for-work after inflation picked up towards the end of the period.

34. **The Progress Report rightly recognizes the need to develop a strategy to better manage the numerous economic, social, environment and natural disaster risks, and to protect the most vulnerable groups.** This strategy is urgently needed. Although social protection for the vulnerable groups is an axis of the PRSP, the role of public safety nets within Madagascar's overall social protection system is not clearly defined. The current system of safety nets has evolved in response to various crises, and as a consequence, much of today's spending appears to be crisis-driven to the detriment of longer term strategic aims. Setting clear standards and objectives based on an assessment of the priority areas of vulnerability to be addressed is a first step to optimizing the use of resources. The strategy, which is being developed with Madagascar's key partners, is an ideal opportunity to clarify these standards and objectives, strategic goals and immediate priorities. It will be reviewed during the next annual Progress Report.

III. MONITORING IMPLEMENTATION OF THE POVERTY REDUCTION STRATEGY

35. **The Progress Report elaborates both the institutional arrangements for monitoring the PRSP and updates the 31 core indicators (Table 6), which monitor progress along the three strategic axis of the PRSP and towards the attainment of the Millennium Development Goals.** The Progress Report maintains the 31 core

indicators, and complements them with five intermediate indicators per Ministry which allow for progress to be monitored on a periodic basis (monthly, quarterly or semi-annual). The staffs welcome the improvement in the indicators for the Ministries of Education and Health which reflect service delivery outcomes better, (e.g., the student-teacher ratio; repetition rates; and for health, outpatient utilization rate), and the agreement reached between the Government and the development partners on these indicators. But the staffs reiterate their recommendation to review the indicators and establish more clearly how the indicators and objectives are derived from the policy measures and sector investment programs in the PRSP.

36. **The Progress Report presents a costed action plan for the Statistics Office (INSTAT) for the next three years (2004-2006).** The staffs recommend that this action plan be assessed to ensure that it responds to the needs for monitoring the PRSP and that adequate resources be allocated to INSTAT to implement the plan.

37. **The staffs recommend clarifying the institutional structure for monitoring and evaluation and developing a capacity building plan, for Secretariat Technique à l'Ajustement (STA), INSTAT, and key sector ministries, to enable these institutions to undertake their functions.** The STA, which is responsible for co-ordinating inputs from the line ministries, and preparing the Progress Report, has organized meetings on a quarterly basis for the existing thematic PRSP working groups. As noted above, a six monthly report was widely disseminated in the capital and six regional workshops. Feedback from these workshops is reflected in the final version of the Progress Report. The Annual Progress Report has been distributed to a wide spectrum of society, including to the ministries, civil society, members of the parliament, and development partners. The options for using existing national processes to report on the implementation of the poverty reduction strategy will also be examined, with a view to improving the alignment of these documents.

IV. RISKS

38. **As noted in the previous JSA, there are several risks that could undermine successful implementation of the poverty reduction strategy.** These risks remain valid today. First, as noted above, Madagascar remains vulnerable to external shocks, including cyclones, droughts, and terms of trade shocks, which present a risk to growth and poverty reduction. Second, continued political stability and a stable macroeconomic environment remain critical to successful implementation of the PRSP. In particular, it is essential that inflation be contained, and pressures to grant generalized wage increases be managed. Third, any delay in implementing the reforms in areas of public finance, institutional development, and capacity building could hamper poverty reduction efforts, as these reforms are necessary to improve public sector efficiency. Fourth, capacity, at different levels of Government to implement and deliver on the ambitious reform program could be a limiting factor. In this regard, staffs would also recommend that Madagascar works toward strengthening its debt management capacity. Fifth, sustainable poverty reduction will depend on attracting private investment into the labor-intensive manufacturing sector and into agro-businesses with spread effects to rural areas. The ability to capitalize on stronger competitiveness gained with the depreciation of the

exchange rate will depend on improving the functioning of customs, macroeconomic stability and managing inflation. Sixth, strong financial support and alignment of the donors around the PRSP is needed to attain the ambitious PRSP objectives, and there is a risk of under-funding if this support is not forthcoming.

V. CONCLUSIONS

39. **The staffs conclude that Madagascar has made good progress in implementing its poverty reduction strategy.** Growth rebounded after the 2002 crisis, and despite the adverse external shocks, is expected to be around 5 percent in 2004. Especially important for the poor, growth in the agricultural sector has been strong. Access to roads has improved. Primary school enrollment rates have increased significantly, and infant and child mortality rates have dropped. Important institutional and legislative reforms in public expenditure management and in fighting corruption have taken place over the last year, which should lead to better allocation and more efficient use of resources.

40. The staffs of the World Bank and the IMF consider that Madagascar's efforts towards implementation of the strategy provides sufficient evidence for its continuing commitment to poverty reduction, and therefore the strategy continues to provide a credible framework for Bank and Fund concessional assistance and for reaching the completion point under the enhanced HIPC initiative. The staffs recommend that the respective Executive Directors of the IMF and the World Bank reach the same conclusion.