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External Assistance and the Peace Process in El Salvador

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Summary. — External assistance has played a critical role in the Salvadoran peace process. Yet the priorities of the donors have often diverged from those of the Peace Accords. Moreover, several major external assistance actors — notably the international financial institutions — have failed to exercise "peace conditionality": they have not used formal performance criteria or informal policy dialogue to encourage the timely implementation of high-priority peace programs and the mobilization of greater domestic resources for this purpose. These institutions have recently broadened their mandates to encompass military expenditure reduction and good "governance." While these concerns are particularly germane in countries emerging from civil war, the case of El Salvador demonstrates that they have yet to be fully incorporated into actual practice.

1. INTRODUCTION

External assistance has played a critical role in El Salvador's peace process. Grants and loans from bilateral and multilateral agencies have been the main source of finance for many programs mandated by the Peace Accords, including the land transfer program, the reintegration of excombatants, poverty alleviation programs, and infrastructure projects. External assistance actors have also influenced the political momentum of the peace process. Aid has affected not only the balance of payments, but also the balance of power.

Aid can be an important complement to limited domestic resources. It can, however, also become a substitute for them. In attempting to ensure that their assistance "crowds in" domestic government spending, rather than supplanting it, donors often seek to make their aid conditional on policy actions by the recipient government, including expenditure commitments. At the same time, the donors know that some programs will not succeed in the absence of external finance. Hence they must strike a delicate balance.

This dilemma has been clearly apparent in El Salvador. External assistance unquestionably has contributed greatly to postwar reconstruction and to the consolidation of peace. But external assistance actors have been less successful in prompting the government to mobilize greater domestic resources to finance peace programs. Indeed, virtually no internal fiscal reforms were undertaken specifically with a view to financing the peace.

This article analyzes the mobilization of external resources for the Salvadoran peace process in both financial and political terms. Section 2 reviews data on external assistance: how much has been provided, by whom, and for what purposes. These data reveal striking discrepancies between the priorities established under the Peace Accords and those of many donors. Several possible explanations for these discrepancies are considered.

Section 3 examines aid conditionality, including formal performance criteria and informal policy dialogue. The absence of conditions can be as critical as their presence. If access to external resources is conditional on the fulfillment of commitments under the Peace Accords, the political resolve of internal actors to maintain the momentum of the peace process can be strengthened. If, on the other hand, external resources are provided without such conditions, the political will to implement difficult but necessary measures may be weakened: aid can ease internal pressures for action, fortify the capacity of reluctant parties to resist those pressures, or divert attention and resources to other issues. In this respect, the record of the external assistance actors in El Salvador has been mixed.

In conclusion, section 4 offers recommendations

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for economic policy in El Salvador specifically and during postconflictual transitions more generally.

2. OFFICIAL EXTERNAL ASSISTANCE

(a) *Resource commitments*

In March 1992, two months after the signing of the Salvadoran Peace Accords, the Consultative Group (CG) for El Salvador met in Washington, DC. The Government of El Salvador's team was led by the Planning Minister, who made it clear that the Government expected the external assistance actors to finance the costs of peace:

> Minister Lievano de Marques emphasized that the reconstruction effort would not be used as a pretext for abandoning disciplined macroeconomic policy. She stressed that the government seeks to finance the effort with foreign assistance and noted that she hoped the funding would be additional, thus allowing the Government to continue its important efforts in redressing other social and economic needs (World Bank, 1992b, p. 5).

In the words of a US official, the Government's stance was, "If you want it to happen, you pay for it."[1]

The donor response was substantial. Since the signing of the Accords, El Salvador has received about $400 million per year in external assistance from bilateral and multilateral agencies. Table 1 presents a breakdown of total commitments for 1992–95 by donor, as reported by the UNDP.[2] These data include aid not specifically related to the Peace Accords. Among the bilaterals, the largest donor was the United States, accounting for more than three-quarters of bilateral aid in 1992–95. Among the multilaterals, the Inter-American Development Bank (IDB) has been the largest single donor.

Table 1. *Official external assistance to El Salvador, 1992–95**

Source of Funds	
U.S.	535.9
Germany†	75.4
Japan	19.7
Italy†	17.0
Spain	16.7
Canada	14.1
Sweden	11.0
Norway	5.1
Netherlands	1.5
Others	2.5
Bilateral subtotal	698.9
IDB	558.8
CABEI	119.8
World Bank	100.3
EEC†	82.7
WFP	39.4
UNDP	7.4
PAHO/WHO	6.1
IFAD	5.0
UNICEF	3.3
Others	6.5
Multilateral subtotal	929.4
Total	1628.3

*Completed, ongoing, and planned projects, US$ million.
†Imputed from data on total project costs (see Text note 2).
Source: UNDP (1994, pp. 3–4).

Table 2 presents data on the financing of specific programs mandated by the Peace Accords for 1993–96. Estimated funding needs, and the categorization of programs into higher and lower priority, are drawn from the Government of El Salvador's report to the April 1993 CG meeting. In the case of poverty alleviation programs, the data refer to the National Reconstruction Plan (NRP) zones only. In the case of infrastructure, no attempt was made to separate out that component directed to NRP areas; the data thus refer to infrastructure projects in the country as a whole. Estimated funding needs totaled $1.8 billion. The government's commitment of domestic resources to these programs was $408 million. Two sets of data on external funding are reported: the first is drawn from the same report to the CG meeting; the second, drawn from on a January 1994 report by the US General Accounting Office (GAO), includes some additional subsequent commitments but provides a less detailed programmatic breakdown. Donor commitments reported by the GAO totaled $739 million, leaving a funding gap of $682 million.

Speaking in September 1994 before the UN General Assembly, Salvadoran President Calderón Sol stated:

> The offer for assistance made by the international community for the implementation of the Peace Accords raised great hope in our country. Part of this has been delivered, for which we are very grateful. However, some has not yet materialized . . . and could be the cause of unnecessary social tensions (El Salvador Information Project, 1994).

Table 3 reports the estimated shortfalls for a number of higher priority programs at that time.

The need for further external resources was reiterated in January 1995 by Salvadoran Vice President Enrique Borgo Bustamante, speaking at the United Nations jointly with Salvador Sánchez Ceren, the secretary-general of the FMLN. Citing a $137 million shortfall, the Vice President said:

> Peace is not enough. We need social peace. We need to remake whatever was El Salvador. We need to walk that last part of the road, and we feel so short of breath.

Table 2. *Funding requirements and commitments for programs mandated under the Peace Accords, 1993–96 (millions of US dollars)*

			External Assistance Commitments and Financing Gap									
			As of March 1993							As of January 1994		
Program	Estimated Requirement	GOES Commitment	U.S.	Germany	Japan	IDB	EEC	Others	Gap	U.S.	Others	Gap
Democratic Institutions	256.6	169.3	19.0				0.5	0.6	67.2	19.0	1.7	66.6
Judicial system strengthening	219.8	162.3	15.0						42.5			
Human Rights Ombudsman	16.8	6.4					0.5	0.6	9.3			
Elections Tribunal	20.0	0.6	4.0						15.4			
Police	277.7	63.4	10.9					5.0	198.4	25.8	6.5	182.0
Public Security Academy	104.7	28.0	4.9					5.0	66.8			
National Civilian Police	173.0	35.4	6.0						131.6			
Land Bank	142.5	23.3	35.0				12.5		71.7	44.0	12.5	62.7
Support to Demobilized Personnel	174.3	3.3	20.0	12.5					138.5	35.0	20.9	115.1
Agricultural credit	62.0	0.0	10.0						52.0			
Housing	77.1	2.6		12.5					62.0			
Microenterprise credit	27.0	0.0	10.0						17.0			
Pensions for disabled	8.2	0.7							7.5			
Poverty Alleviation (NRP only)	310.2	57.2	94.5			34.4	18.8		105.3	106.1	53.2	93.7
Housing	76.2	40.9				15.8			19.5			
Municipalities in Action	65.2	0.0	62.5						0.0			
Maternal and child health	55.3	5.3	8.0				12.0		30.0			
Social Investment Fund	52.6	4.8				18.6			29.2			
Other	60.9	6.2	21.3				6.8		26.6			
Subtotal: Higher priority	**1161.3**	**316.5**	**179.4**	**12.5**		**34.4**	**31.8**	**5.6**	**581.1**	**229.9**	**94.8**	**520.1**

— continued overleaf

Table 2. *Continued*

			External Assistance Commitments and Financing Gap									
			As of March 1993							As of January 1994		
Program	Estimated Requirement	GOES Commitment	U.S.	Germany	Japan	IDB	EEC	Others	Gap	U.S.	Others	Gap
Productive and Social Sectors and Human Capital	120.0	10.9	25.7	5.5	3.8		3.7	16.4	53.5	44.1	79.6	(14.6)
Productive sector	55.5	4.8						9.7	41.0			
Programs for disabled	14.6	2.0	8.9				3.7		0.0			
Scholarships for demobilized	16.5	1.5	9.5	5.5					0.0			
Other education and training	20.7	2.6	7.3						10.8			
Other	12.7				3.8			7.2	1.7			
Infrastructure	530.1	78.3	20.5		93.1	161.7		6.0	170.5	30.0	260.8	161.0
Energy	287.6	48.6			63.0	142.7		5.0	28.3			
Roads and bridges	162.3	17.4			20.1				124.8			
Water	34.0	4.0			10.0	19.0		1.0	0.0			
Other	46.2	8.3	20.5						17.4			
Environment	17.5	1.9							15.6		0.2	15.4
Subtotal: Lower priority	**667.6**	**91.1**	**46.2**	**5.5**	**96.9**	**161.7**	**3.7**	**22.9**	**239.6**	**74.1**	**340.6**	**161.8**
Total	**1828.9**	**407.6**	**225.6**	**18.0**	**96.9**	**196.1**	**35.5**	**28.5**	**820.7**	**304.0**	**435.4**	**681.9**

Sources: MIPLAN (1993, pp. 49–63); GAO (1994, p. 5).

Table 3. *Funding shortfalls for higher priority programs as of September 1994 (millions of US dollars)**

Program	Needed	Available	Shortfall
Armed Forces demobilization	31.0	25.0	6.0
Public security			
National Police demobilization	9.8	0.0	9.8
Other programs	1.0	0.0	1.0
Land programs			
FMLN land transfer	97.1	78.7	18.4
FAES land transfer	42.5	29.1	13.4
Agricultural credit	44.2	18.9	25.3
Technical assistance	1.1	0.0	1.1
Reinsertion of excombatants			
Microenterprise credit and technical assistance	11.7	8.1	3.6
Scholarship program	14.8	14.8	0.0
Leaders and mid-level commanders program	4.1	0.0	4.1
Wounded combatants program	11.1	0.4	10.7
National Police reinsertion	16.5	8.0	8.5
Total	**284.9**	**183.0**	**101.9**

*Not all higher priority programs are included. For example, estimates for the human settlements program were unavailable, but it is believed that these would significantly increase the total deficit.
Source: Data provided by the Ministry of Planning, Government of El Salvador.

At the same time, government officials maintained that "they cannot provide any more money without levying new taxes or cutting into education and health programs" (Crossette, 1995). There remains, however, considerable scope in El Salvador both for increasing tax revenues and for shifting government expenditures from other uses besides education and health.

The fact that a substantial, and increasing, fraction of external assistance to El Salvador takes the form of loans rather than grants is a further reason to intensify efforts to mobilize domestic resources to finance peace programs and public investment. More than 40% of foreign finance for peace-related programs has come in the form of loans, primarily for infrastructure projects. Loans in general — and loans from international financial institutions in particular — must one day be repaid with interest.[3] Positive net transfers on debt today lead inexorably to larger negative net transfers tomorrow; that is, debt service payments (interest and amortization) must eventually surpass new borrowing. The question is not if this will occur, but when.[4] It would be an unfortunate irony — and, in light of the potential for greater domestic resource mobilization, an unnecessary one — if El Salvador's postwar reconstruction efforts were to sow the seeds of a future debt crisis.

(b) *Donor priorities*

The data in Table 2 suggest striking discrepancies between the priorities defined by the government (in consultation with UN and US officials) and the priorities of the major non-US donors as revealed by their financial allocations. This is attributable not only to the fact that individual donors had their own agendas, but also, in part, to the fact that the government's own priorities were not always clearly established. While the government and the US allocated more than 75% of their funding to "higher priority programs" — the National Civilian Police (PNC), judicial and democratic institutions, the land transfer program, the reintegration of excombatants, and poverty alleviation programs — the other donors devoted 78% of their funding to "lower priority programs." Funding from non-US donors for the PNC, judicial and democratic institutions, and land transfer amounted to only $21 million; together, these programs had an expected shortfall of $311 million. At the same time, these donors committed $261 million to physical infrastructure. If we had comparable data on external assistance for non-Peace Accord programs, the apparent divergence in priorities would be even sharper.[5]

Several factors may help to explain the reluctance of donors to commit greater financial resources to the programs mandated by the Peace Accords: (i) constraints on the aggregate volume of aid; (ii) the "free-rider" problem in coordination among aid donors; (iii) legislative, political, and institutional impediments to the funding of certain types of activities; and (iv) skepticism regarding the likelihood that programs will succeed. These factors are not mutually exclusive, and their relative weight varies among donors and across programs.

(i) Aggregate constraints

In the 1990s, worldwide official development assistance began to contract, as donor governments curtailed foreign aid programs in response to fiscal constraints and changing domestic priorities.[6] At the same time, Eastern Europe and the former Soviet states began to compete for external assistance. Moreover, with the end of the Cold War, the national security motivation for US foreign aid in Central America and elsewhere waned. Together, these factors led to a 44% cut in US economic assistance to Central America during 1991–93, and to a further 42% cut in 1994.[7]

For the United States, however, El Salvador remains a high priority country. El Salvador was the fifth largest recipient of US aid in the 1980s (after Israel, Egypt, Turkey, and Pakistan),[8] and in the 1990s it has continued to receive more US aid than any other country in Latin America, virtually all of it in the form of grants. The signing of the Salvadoran Peace Accords was also followed by a large influx of new lending by the multilateral development banks. Compared to other countries, therefore, El Salvador has retained a rather generous slice of the aggregate external assistance pie.[9]

(ii) The free-rider problem

Insofar as foreign aid is intended for developmental and humanitarian purposes, it has the qualities of a public good. If one donor provides assistance, all reap the "benefits." Individual donors, particularly those with relatively modest budgets, may believe that their own marginal impact is negligible: it is the decisions of the other donors which determine the humanitarian or developmental outcome. Hence donor governments may be tempted to "free ride" on the assistance provided by others, devoting their own resources to less disinterested purposes.[10] Aid coordination mechanisms, such as the Consultative Groups, provide a means to defuse this problem, but their effectiveness is a matter of degree.

In El Salvador, the overwhelming preponderance of US official assistance during the war years both simplified and complicated matters. Alone among the donors, the United States had both an established institutional presence in El Salvador and a broad vision of a desired course of political and economic reform. The United States responded quickly to the signing of the Peace Accords and indeed, helped to design the NRP prior to the signing of the Accords. The United States had accumulated large reserves of local currency during the war, as counterpart funds for its Economic Support Fund (ESF) and food aid (Public Law 480) programs, and these provided a ready and flexible source of cash.[11] In addition, US Agency for International Development (USAID) had a number of ongoing development projects which could be redirected toward the reconstruction effort.

Many other donors, by contrast, had no substantial on-the-ground presence in El Salvador at the time of the signing of the Accords. Moreover, there was a sense among some of them that the United States, having done so much to finance the war, now bore the main responsibility for financing the costs of peace. At the same time, however, the US government sought to encourage other agencies — notably the United Nations and the international financial institutions (IFIs) — to invest resources in El Salvador's peace process and postwar reconstruction effort. On balance the US presence may have "crowded in" more external assistance to postwar El Salvador than it "crowded out."

(iii) Legislative, political, and institutional impediments

Certain types of assistance are difficult for some donors to provide. Assistance to police forces, for example, is legally barred by some donor governments. The purchase of land for redistribution may face domestic political opposition, both from critics of land reform and from critics of compensation to former landowners. Multilateral development banks, which have traditionally financed physical infrastructure and, more recently, "social" programs, may regard the strengthening of democratic institutions as an activity outside their mandate or competence. These impediments do much to explain the apparent discrepancies between donor priorities and those of the Salvadoran Peace Accords. In the absence of reassessment and reforms in the external assistance agencies, similar discrepancies are likely to recur other postconflictual settings.

The main source of external assistance for El Salvador's new National Civilian Police force has been the United States. Since USAID is prohibited by law from providing direct assistance to police forces, this required a special arrangement. With the permission of Congressional oversight committees, USAID transferred the funds in question to the State Department, which then contracted the Justice Department to provide assistance through its International Criminal Investigation and Training Act Program. The governments of Spain, Sweden, and Norway also provided some support to the PNC. But for many donors, police funding remains politically untouchable. The fear is that the police will become involved in political repression and human rights abuses. Yet a central aim of the creation of the PNC was precisely to guard against such eventualities.

More generally, institution-building is a slow process, often more intensive in time than in money. "There are two types of donors," commented a donor official, "those with patience and little money, and those with no patience and plenty of money." The strengthening of democratic institutions appeals more to the former type of donor than to the latter.

Much of the infrastructure assistance received by El Salvador in recent years is not directly related to the consolidation of peace. Rather it is the kind of lending which would have taken place had there never been a war, although the volume of loans after the signing of the Peace Accords was perhaps augmented by pent-up supply, since much lending was deferred during the war. Some postwar infrastructure lending was redirected toward the exconflictive zones, but in most respects these projects represent business as usual.

Donor preferences for "trade-related" assistance may help to explain the relatively generous funding of physical infrastructure as opposed to higher priority programs under the Salvadoran Peace Accords. A common objective in external assistance programs — in some instances the overriding one — is the promotion of exports from the donor country. Such tied aid not only inflates nominal project costs (since the same inputs often could be obtained on the world market at a lower price), but also biases assistance toward "projects requiring major imports in areas of particular export interest to the donor" (OECD, 1985, cited by Jepma 1994, p. 73).

External assistance provided for one purpose can free domestic resources for other purposes. Such "fungibility" means that aid earmarked for lower priority programs could indirectly help to finance high-priority programs by easing competing demands on the government budget. This assumes, however, that the government would have otherwise felt compelled to finance those lower priority activities, and that the government reallocates any resources so liberated to peace programs. Neither assumption is self-evidently true.

Balance-of-payments support — whereby the government receives hard currency, sells it to importers, and can then use the local currency proceeds as it wishes — is particularly fungible. Furthermore, such loans can be disbursed much more quickly than project lending. The conditions attached to balance-of-payments assistance in El Salvador, as elsewhere, have centered on macroeconomic stabilization and structural adjustment. The possibility of using such aid to finance Peace Accord programs was recognized, however, in the World Bank's Second Structural Adjustment Loan.[12] Germany's decision to contribute $9 million in cofinancing for this loan was reportedly prompted by this consideration.

Although the institutional impediments to direct support of Peace Accord programs by some major donors, including the IFIs, are formidable, they are not insurmountable. In a precedent-setting departure from its usual project profile, the IDB is currently considering a $20 million loan to El Salvador to support the judicial reform. Such a loan would, in effect, expand the notion of "infrastructure" considered appropriate for IDB lending beyond the traditional foci on physical works and human capital investment to include the strengthening of democratic institutions. This suggests that the logic of the Salvadoran peace process has the potential to catalyze institutional change in the IFIs themselves, with implications extending well beyond El Salvador.

(iv) *Donor skepticism*

Skepticism among some donors as to the government's political will to comply fully with the letter and the spirit of the Peace Accords may have posed a further constraint on the mobilization of external resources.

From the outset of the peace negotiations, there were two opposing views as to how aid should be channeled to intended beneficiaries in the exconflictive zones. The US position was that aid should flow through the sovereign government. The government likewise was keen to avoid any powersharing with the exguerrillas. In the words of a donor official involved in the negotiations:

> The government wanted some consultation, but nothing so participatory as to be co-government. They didn't want to repeat the Nicaraguan experience. They kept using the phrase "*co-gobierno*" as something to be avoided.

Other donor officials, particularly from some of the European bilateral agencies, believed that at least part of the aid to the exconflictive zones should be channeled outside the government, for example, through nongovernmental organization (NGOs) which had worked in these areas during the war. With intimate knowledge of the local terrain and established links to communities, the NGOs were seen as a valuable complement to the state. The UN-brokered compromise allowed some aid to be channeled through the UNDP and NGOs, but the vast bulk of reconstruction aid has been channeled through the government.[13] Concerns over politicization in the distribution of these resources may have dissuaded some donors from providing greater support.

In interviews, a number of donor officials expressed concern about the El Salvador government's unwillingness to commit greater domestic resources to peace programs, and cited this as a reason for their own reluctance to do so. "The priorities of the government should be reoriented in favor of constructing an acceptable social infrastructure," said one. "The government should not leave responsibility for this to the donors." Another official took the view that the relatively large allocations of external assistance to physical infrastructure projects reflected the actual (if not stated) priorities of the government as well as of some major donors.

Several officials expressed particular skepticism about the government's commitment to the creation of the new National Civilian Police. On the PNC's equipment needs, one remarked:

> We have no tradition of handing out weapons. But the Salvadoran army has huge stocks, even though some of these are not easy to use for civilian purposes. The army has vehicles, too. Many needs of the PNC could be met by taking from the army. This is a political question: how to persuade the army to give up equipment. We do not want to help the army hold onto its equipment by financing purchases for the PNC.

The government's reluctance to finance even mundane items for the PNC, such as soap and towels, reinforced this skepticism.

Such reservations are grounded in the specific circumstances of El Salvador. But similar problems can be expected in other postconflictual settings. Peace accords may end the shooting, but the divisions which precipitate civil wars do not vanish instantly. They constitute the setting — and the challenge — for the consolidation of the peace.

3. PEACE CONDITIONALITY?

In development circles, "conditionality" often is regarded as something of a dirty word. As Schoultz (1989, p. 410) remarks, "many observers reject as unethical and perhaps immoral the notion of establishing conditions upon aid disbursements." Some external assistance agency officials are reluctant even to discuss the matter. "We have no conditionalities on our assistance," insisted a senior EEC official interviewed for this study. But he then added: "Our only conditionality is respect for democratic institutions." As the qualification suggests, the absence of conditionality can be as problematic as its presence.

Aid conditionality is here taken to be a fact of international life. The issue is not whether external assistance actors should wield power, but rather what they do with it.[14]

In general, balance-of-payments assistance affords scope for broader conditionality than does project assistance: the conditions govern what the recipient will do not with the money but in return for it. In El Salvador, the external assistance actors most able to exercise conditionality, by virtue of the volume and types of assistance at their disposal, have been the United States, the World Bank, the IMF, and the IDB.[15] Accordingly, this section focuses on their policies.

(a) *Macroeconomic conditionality*

In El Salvador, as elsewhere, the primary goals of aid conditionality in recent years have been macroeconomic stabilization and structural adjustment. These are not the only goals conceivable in theory, nor are they the only ones that major external assistance actors ever embrace in practice. Other goals which have been discussed, and at times pursued, include poverty reduction, good governance, and reductions in military expenditure. While these other goals seem particularly germane to countries in postconflictual transitions, they have not featured prominently in aid conditionality in El Salvador.

Since 1989, there has been a close correspondence between the macroeconomic policy preferences of the Government of El Salvador and those of the donors. Both parties favored government budget deficit reduction, low inflation, privatization of the financial sector and of agricultural exports, trade liberalization, and streamlining of the state. The macroeconomic conditionalities embodied in the World Bank's Structural Adjustment Loans (SALs) and IMF stand-by arrangements therefore have not been impositions on a recalcitrant government.

"In both SALs, the government came to us with the program," recalled a World Bank official. "We just worked out the details. Of course, we were very happy with what they proposed. But there is nothing in these agreements that we invented." An IMF official described target-setting in El Salvador as a "very iterative" process: "We're on the phone with them a lot. We're dealing here with a government that shares the same philosophy." In a reversal of the conventional scenario elsewhere, the government in some instances proposed tighter targets than were initially suggested by the Bretton Woods institutions. Nothing precludes a government from pursuing tighter targets on its own. But their inclusion in formal agreements with the World Bank and the IMF can serve to deflect criticisms of unpopular measures to the external agencies.

The close working relationships between IFI officials and their counterparts in the government of El Salvador are not unusual. Jacques Polak (1991, p. 66), the former Economic Counsellor of the IMF, remarks:

> The country's team, typically composed of senior treasury and central bank officials, will often seek alliances with the Fund staff in order to strengthen its own policy prescriptions. Not infrequently, letters of intent contain commitment put there only because the country wanted them.

In the case of multilateral development banks, there is a further basis for alliances: the job of bank officials is to make loans, and the job of government officials is to obtain them. Congenial relationships carry the risk of "clientitis," a sense of identification which inhibits lending institutions from proposing and implementing conditionalities not welcomed by the borrower.

(b) *Economic stabilization v. political stabilization*

The goals of economic stabilization and political stabilization are complementary: in the long run neither is possible without the other. In the short run, however, conflicts between these objectives can arise and pose difficult tradeoffs.

One evident possibility is that in the absence of adequate external finance, budget deficit targets may be incompatible with the need to fund peace-related programs. An August 1993 study on the "Economic Consequences of Peace in El Salvador," undertaken by the secretariat of the UN's Economic Commission for Latin America and the Caribbean, concluded:

> [I]t might be necessary to explore the possibility, should the situation arise, of slightly extending the deadline for reducing inflation or of pursuing trade liberalization less vigorously. Within limits, setting more flexible quantitative goals for the stabilization programme might be an acceptable sacrifice, since it would secure the higher goal of ensuring the governability of a society that has, for years, been in the throes of a disastrous civil war (CEPAL 1993, p. 12).

When queried on this point, IFI officials offer two responses: first, a relaxation of budget deficit targets would jeopardize macroeconomic stability, ultimately endangering the peace process itself; and second, in practice the budget constraint has not been binding in El Salvador. Neither argument can be lightly dismissed.

The first argument proceeds from the assumption that larger government budget deficits would trigger higher inflation. This would reduce the competitiveness of the export sector (given a *de facto* policy of maintaining a fixed exchange rate), and would harm the poor who are least able to maintain their incomes in the face of rising prices. Hence IFI officials stress the need to finance peace expenditures by other routes: via increased tax revenues, government expenditure shifting, and external resources.

There is a large intermediate terrain, however, between rigid adherence to the macroeconomic targets on the one hand, and profligate deficit financing of peace-related expenditures on the other. Analogous to the familiar tradeoff between inflation and unemployment depicted in macroeconomics textbooks, there may be a tradeoff between the size of the government budget deficit on the one hand and the social tensions arising from inadequate peace expenditures on the other. This situation is depicted in Figure 1.[16] Faced with such a tradeoff, prudent policy making does not restrict the choice set to points *A* and *Z*.

The second argument points to government fiscal priorities, rather than the aggregate expenditure ceiling, as the explanation for inadequate funding of peace programs. This argument is well founded: there is considerable scope in El Salvador for both expenditure shifting and increasing tax revenues. But this raises a further issue. If economic development is the overriding objective of the IFIs, if the consolidation of peace is necessary to economic development, and if successful and timely implementation of the programs

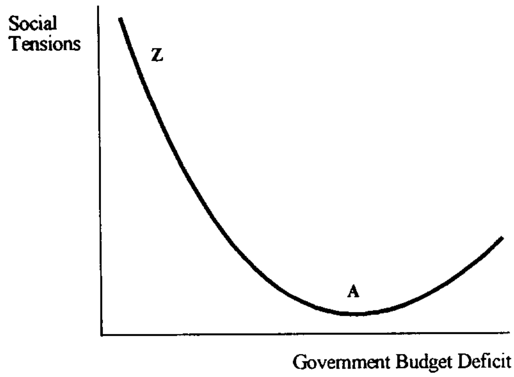

Figure 1. *Tradeoff between government budget deficit and social tensions due to inadequate peace expenditures.*

mandated by the Peace Accords is necessary for the consolidation of peace, then it logically follows that the IFIs should include the latter in their conditionalities.

Yet in El Salvador the IFIs have for the most part limited their purview to more conventional macroeconomic concerns. They have not extended their conditionalities to the peace process, for example, by setting targets for greater reallocation of government spending to programs mandated by the Peace Accords. Instead the IFIs have supported the government's efforts to shift the costs of peace onto the external assistance agencies. The World Bank (1992a, p. 9) set the tone at the March 1992 CG meeting:

> Adequate external financial support for the NRP [National Reconstruction Plan] is the critical condition for NRP's implementation within a framework of macroeconomic stability and sustainable growth. Without sufficient external resources the Government will face two alternatives: (i) maintain macroeconomic stability by curtailing NRP implementation, with likely severe political and social consequences or (ii) finance the NRP predominantly with domestic resources sacrificing macroeconomic stability and longer-term growth.[17]

This statement again reduces the potential tradeoff between macroeconomic instability and inadequate peace expenditures to a binary all-or-nothing choice; and, more important, it ignores the scope for further reallocation of domestic resources to peace programs.

Faced with the fiscal requirements of peace, and limited external resources, the government in fact has three options: to run a larger budget deficit; to increase domestic resource mobilization by shifting government expenditure from other uses and/or increasing tax revenues; and to accept shortfalls in the funding of peace-related programs. In postwar El Salvador, the second option has much to recommend it. While there is some limited room for easing the budget deficit targets, excessive relaxation would prove costly in terms of macroeconomic stability. There is considerable scope, however, for further mobilization of domestic resources to finance the costs of peace.

(c) *Military expenditure*

Military expenditure is an obvious candidate for budget cuts to free more domestic resources for programs mandated by the Peace Accords. Although Salvadoran military spending has declined since the war, it continues to absorb a substantial amount of scarce government resources. The share of Salvadoran GDP devoted to the military in 1993 was 1.7%, according to the IMF (1994, p. 45).[18] This compares unfavorably with the 0.5% for health and 1.6% for education (see Table 4), and remains far above its prewar level of 0.7% of GDP.[19]

According to a senior IMF official interviewed for this study, the Fund has not engaged in discussions of military expenditure in El Salvador.[20] Instead the Fund has maintained its traditional focus on aggregate government expenditure rather than its composition: "We tend to leave that [expenditure composition] to the World Bank and IDB. When asked, we make certain analyses, for example, of the share of the wage bill in the public sector. But generally we rely on others."

A World Bank official closely involved with El Salvador policy stated that the Bank "never discussed explicitly" the issue of defense expenditure. This official maintained that the issue lies outside the Bank's mandate and competence, and that a change in the Bank's mandate in this respect would be undesirable, as it "would risk damaging the credibility of the Bank as an objective, apolitical institution."[21]

An IDB official expressed the view that donor pressure on the Cristiani government would have been counterproductive:

> There are political realities. The Peace Accords were delayed by Cristiani's problems with the military. I have no doubt that he would have liked to cut their budget more, but those guys are powerful. Had Cristiani not been able to postpone the sacking of 100 top military officers, the peace process might be in shambles now.

Following the signing of the Peace Accords, US military aid was scaled down to $23 million in the year 1992.[22] Cutbacks in US military aid were accompanied by substantial US funding for Peace Accords programs, as documented above. Initial US conditionalities were not as strong as they might have been, however. "We could have leveraged more from the government in the early 1990s, on land, the PNC, and other peace-related issues," a US official remarked. "Our policy at the time was that we were getting as much as we should extract. I personally believe we could have gotten more, but we ourselves didn't have the political will." The situation changed somewhat under the Clinton administration (that is, after January 1993), but at the same time the volume of US aid decreased.

The efficacy of recent US pressures on the government has also been limited by the lack of support from the IFIs. While the World Bank, IDB, and USAID have negotiated crossconditionality on macroeconomic issues, they have not done so with respect to implementation of the Peace Accords. A senior USAID official stated that he personally approached World Bank and IDB officials to seek backing for efforts to reorient government spending toward Peace Accord programs, without success:

> The IFIs have steadfastly refused to talk about military expenditure targets in El Salvador. They say: "This is political conditionality, and we are apolitical organizations. We cannot include budgeting sufficient funds for the PNC or land transfer in our conditions. The U.S. government can do that because it has a political agenda, but we don't." There has been a concerted effort by the Banks to stay completely away from these issues.

The reluctance of the IFIs to venture into this terrain in El Salvador is not entirely consistent with the public posture of these institutions. There has been much debate in recent years as to the appropriate policies and role of the IFIs with respect to military expenditures.[23] In an April 1991 address to a World Bank conference, former World Bank President Robert McNamara called for reductions in military expenditures in developing countries and endorsed the use of conditionality to further this goal (McNamara, 1992). In December of the same year — a month before the signing of the Salvadoran Peace Accords — newly retired World Bank President Barber

Table 4. *IMF estimates of central government expenditures on the military, education, and health, 1989–93 (percentages of GDP)*

	1989	1990	1991	1992	1993
Military	3.7	3.0	2.6	2.2	1.7
Education	1.8	1.6	1.5	1.5	1.6
Health	0.8	0.8	0.8	0.8	0.5

Source: IMF (1994b, pp. 26, 45).

Conable, Jr., called on the international community to present a "united front" against excessive military spending:

> Weak or uncertain civilian governments may publicly protest, as invasion of their sovereignty, admonitions that arms expenditures be reduced. I speak from experience when I say that such pressure may be privately welcomed by the new democracies. It can be a decisive element in strengthening civilian hands in the internal battle to allocate available resources to economic growth and quality of life investments rather than unproductive military hardware.[24]

A December 1991 memorandum presented to its Board of Directors codified World Bank policy and was incorporated in the Bank's operational directives. The memorandum called on Bank staff to "raise issues of unproductive expenditures where they are significant, as part of its policy dialogue and public expenditure reviews, rather than to impose conditionality related to military expenditures" (World Bank 1991a, p. 2). An accompanying opinion by the Bank's General Counsel concluded:

> The discussion of public expenditures for economic and social purposes and the degree of their adequacy for these purposes may therefore be considered . . . as matters relevant to the Bank's mandate, as it is now envisaged, and they obviously fall within the Bank's competence. In addressing these issues, the Bank will be indirectly addressing the issue of non-productive expenditures but without having to get involved in the politically sensitive matter of what is an appropriate level for a country's military expenditures. After all, these are two sides of the same coin (World Bank, 1991b, pp. 2–3).

Although apparently ignored in the case of El Salvador, these guidelines reportedly have been put into practice elsewhere:

> [T]he World Bank has confronted the issue of military expenditure in the case of several countries in which such allocations seemed excessive relative to spending on development programs and when important social and physical infrastructure programs were being starved of resources. Because of the sensitivity of the topic, the dialogue has been at the level of Bank senior management and country leaders (World Bank, 1994a, p. 48).

These have "tended to be countries with a relatively high dependence on external aid flows" (p. 49). An example is Uganda, where reportedly "demilitarization came only after prodding from the World Bank" (Carrington, 1994).

The IMF has also moved in recent years to place military expenditure on its institutional agenda. An April 1991 communiqué of the IMF's Development Committee raised "the need to re-examine the possible reallocation of public expenditure, including excessive military expenditures, to increase their impact on poverty reduction."[25] In the same year, at the joint World Bank/IMF annual meeting, IMF Managing Director Michel Camdessus announced that military budgets are "a proper subject for our attention," and characterized this as "just an extension and intensification of our traditional work to help countries improve their macroeconomic policies."[26]

To this end the IMF staff has produced several research papers examining data on military spending and its economic impact.[27] In addition, according to former IMF Economic Counsellor Jacques Polak, the Fund in a few cases "has exercised pressure to reduce military expenditures as part of a program of fiscal adjustment." Polak explains:

> Action of this nature by Fund missions does not show up in letters of intent and thus does not form part of the Fund's formal conditionality. But the Fund and the Bank can be expected to use their financial clout to steer government finance in client countries from military toward development outlays (Polak, 1991, pp. 29–30).

There appears to be ample space, therefore, for officials of the Bretton Woods institutions to place military expenditure squarely on the policy agenda. The fact that they have failed to do so in El Salvador suggests that the importance of this issue has yet to be widely affirmed within these institutions at the operational level.

Similar room for maneuver is emerging at the IDB, where the new emphasis on social sectors in recent years has led to heightened awareness of the constraints posed by excessive military spending. A recent assessment of its lending program commissioned by the IDB observed:

> It is crucial that the IDB, through policy dialogue and conditionality linked to social sector lending, persuades governments to allocate a higher proportion of *their own spending* to expenditure which favors the poor (and a lower proportion of their spending to, for example, military spending) . . . Tranched disbursements, linked to policy conditionality and especially dialogue, may be particularly effective for encouraging such changes in government spending structure (Griffith-Jones *et al.*, 1993, p. 69; emphasis in original).

Once again, however, there is no evidence that IDB officials have raised the matter of military expenditure in the case of El Salvador.

(d) *Governance*

Turning to the other side of the budget-reallocation coin, it would appear that here, too, there is ample institutional scope for peace conditionality in countries like El Salvador. Whereas the legal framework, judicial reform, and the strengthening of democratic institutions were once regarded as outside the purview of the IFIs, in recent years these have been incorporated into the IFIs' definition of their mandate under the general rubric of "governance."

In April 1992 World Bank President Lewis Preston termed good governance "an essential complement to sound economic policies" (World Bank, 1992c, p. v). The glossy cover of a 1994 World Bank publication titled *Governance* features the terms "legal framework," "military expenditures," "accountability," "participation," "judicial reform," and "human rights." The document states:

> Good governance is epitomized by predictable, open, and enlightened policymaking (that is, transparent processes); a bureaucracy imbued with a professional ethos; an executive arm of government accountable for its actions; and a strong civil society participating in public affairs; and all behaving under the rule of law (World Bank, 1994a, p. vii).

Speaking in June 1994, IMF Managing Director Camdessus similarly included "good governance — that is, publicly accountable and participatory government that serves the interests of all of society rather than sectional interests" as a crucial ingredient in the "recipe for success" in structural adjustment and economic development (*IMF Survey*, 1994, p. 209).

It would appear, therefore, that the central political and military reforms of the Salvadoran Peace Accords fall within the legitimate purview of the IFIs as redefined by these institutions in recent years. Yet the practice of the IFIs in El Salvador has failed to live up to this potential. In their own project lending, the IFIs have contributed nothing to the various high-priority programs mandated by the Peace Accords.[28] Nor have they deployed formal conditionality or informal policy dialogue to support these programs indirectly.

(e) *The role of the United States*

The United States has attempted to wield conditionality on behalf of the peace process in El Salvador with varying degrees of commitment and with mixed results. As early as 1991, the United States included in its ESF program measures to strengthen democratic institutions, especially the judiciary. According to USAID officials, "The combination of conditionality and provision of resources through project assistance increased the allocation of public expenditures to democratic institutions" (Belt and Lardé, 1994, p. 7).

Despite the very large volume of US aid to El Salvador during the war, US influence was circumscribed by the "reverse leverage" wielded by the Salvadoran government *vis-à-vis* the United States. The Reagan administration needed a moderate civilian government in El Salvador to ensure continued US Congressional backing for the counterinsurgency campaign. "As the case of El Salvador suggests," writes Schoultz (1989, p. 415), "at times the donor is more dependent on the recipient than vice-versa." With little credible threat of significant aid reductions, US aid conditionality was less effective than the sums involved might otherwise suggest.

With the end of the Cold War, recipient governments presumably have less scope to wield reverse leverage. Hence while the volume of US aid to El Salvador has diminished compared to the war years, it is conceivable that the effectiveness of US conditionality has been enhanced since the withholding of funds is now a more credible possibility.

As a relatively successful instance of donor leverage, observers cite the US response to the June 1993 appointment of Oscar Peña, former head of the National Police's Narcotics Unit, as deputy director of the PNC. This appointment was widely perceived as a threat to the integrity of the new civilian police force. The United States withheld deliveries of police vehicles and equipment until Peña finally resigned, almost a year later, in May 1994.

In the case of the land transfer program, US leverage has been less effective. The administrative impediments to land transfers — such as the need to ensure that all back taxes on the land have been paid, or that all joint owners (some of whom cannot be traced) sign the various transfer documents — could be removed, for example by Presidential Decree, if there were the political will to do so. Moreover, the land could be transferred as an outright gift, rather than saddling the new owners with a debt for its purchase.

The Salvadoran government has been politically unwilling to take these steps. A US official with long-standing experience in El Salvador explained:

> The smartest and easiest thing they could have done at the beginning would have been to say, "You're farming it? Okay, here is the title." The GOES is not paying anything for the land transfer program — it's all U.S. and EEC money. But the government made it complicated because they don't want to give the opposition a gift. Their attitude is, "We fought these people for twelve years — why should we reward them now?"

Perhaps donor conditionality could have countered this lack of political will. But the United States, the main financier of the land transfer program, chose not to exercise it. "The U.S. was not in any mood to force the government into a land give-away program," recalls the official:

> That would smack of subsidies. And to a lot of people on Capitol Hill, land reform is a dirty word. It's seen as stealing land from one person and giving it to someone else. Of course, in this case that is pretty far from the truth. It's not stealing. You can even compensate the owner, if you can find him. But lack of political will *here in the U.S.* was a problem, too.

The result was a land transfer program "doomed to failure because, quite simply, it is designed to fail."[29]

In sum, during a postconflictual transition external assistance actors must be prepared to exercise "peace conditionality." While the support of the international community has played a crucial role in the Salvadoran peace process, that role could have been strengthened by more active peace conditionality. The conditionalities of major aid donors — in particular, the international financial institutions — for the most part were not deployed in support of such objectives as the reallocation of government spending from the military to the new democratic institutions, or the timely implementation of such key programs as the creation of the PNC and land transfer.

In a sense, then, rather than impeding the consolidation of peace by being "too tight," donor conditionalities failed to advance it, by being "too loose." The need to mobilize more effectively the political resources of the external assistance actors — in addition to their financial resources — is a key lesson of the Salvadoran experience for future cases of postconflictual transition.

4. CONCLUSIONS

External assistance has done much to fund the costs of peace in El Salvador. In general, implementation of the programs mandated by the Peace Accords has not been seriously hampered by a lack of external resources. The explanation for delays must be sought elsewhere, in administrative bottlenecks and inadequate political will, one symptom of which has been the inability or unwillingness of the Salvadoran government to mobilize greater domestic resources for peace-related needs.

El Salvador will need further external assistance in support of peace-related programs in coming years. But a continued willingness on the part of donors to provide resources for the consolidation of peace must be coupled with a greater willingness to withhold them as a penalty for failure to implement provisions of the Peace Accords. To be effective, aid conditionality must be backed by a credible link between funding and the conditions embodied in formal commitments and informal policy dialogue. This linkage is particularly important in the case of peace conditionality, where (unlike macroeconomic conditionality in postwar El Salvador) there may exist differences of interest and philosophy between external assistance actors and the government. In this important sense, aid conditionality must be tighter, rather than looser, in the context of a postconflictual transition.

External assistance actors sometimes conflate a country with its government. Yet the government is clearly only one among several internal political actors. The distinction between the government and the country as a whole is particularly important in the aftermath of a negotiated end to a civil war. In providing postwar assistance, donors must seek to maintain the balance among different internal actors on which the momentum of the peace process depends.

A more active policy of peace conditionality in El Salvador would include formal performance criteria and/or informal policy dialogue with the following objectives:

- Reduction of military expenditure in the next two years to its prewar fraction of GDP, 0.7%.
- Reduction of military expenditure in the next five years to a fraction of GDP similar to that in Mexico and Costa Rica, that is, 0.3–0.4%.
- More vigorous efforts to raise the tax coefficient to 15% of GDP within the next three years and, at the same time, to make the incidence of taxation more progressive. In addition to further improvement in the administration of income tax collection from high-income individuals, such efforts should include taxes on luxury goods consumption (in the case of goods which are exclusively imported, this could be accomplished through tariff policy), and taxes on high-value property transfers.
- The commitment of adequate domestic resources on a priority basis to the National Civilian Police, and the implementation of strict measures to prevent human rights abuses by the new force.
- Steps to streamline and expedite the Land Transfer Program.
- Direct lending in support of the strengthening of democratic institutions, translating concern for "good governance" into tangible action.

In some postconflictual settings, the need to finance peace-related expenditures may require relaxation of macroeconomic conditionalities, for example, if the only feasible way to fund particular programs is through deficit finance. In the case of El Salvador, however, the problem has not been one of insufficient aggregate resources; rather it has been inadequate mobilization and allocation of domestic resources for peace-related needs. Hence there is no compelling argument at present for substantially looser fiscal targets.

During the Cold War, issues of democratic governance and military expenditure were often subordinated to security concerns in the practice, if not always the rhetoric, of the major external assistance actors. The post-Cold War era has seen a pronounced shift in the stated policies of the IFIs, but this shift has yet to be reflected in their actual practice in El Salvador. In this sense, the consolidation of the peace remains an uncompleted task not only in El Salvador, but in the international financial institutions too.

NOTES

1. Unless otherwise noted, all quotations are from interviews with officials of external assistance agencies conducted in New York, Washington, DC, and San José, Costa Rica, in October and November 1994.

2. In addition to 1992–95 assistance, the UNDP reports "total project cost," which includes expenditures prior to 1992 for projects begun before the signing of the Peace Accords. In the cases of Germany, Italy, and the EEC, only total project cost is available. German and Italian assistance for 1992–95 is here estimated by multiplying their total project costs by the average share of these years in the total project costs of other bilateral donors (48.9%). EEC assistance for 1992–95 is similarly estimated using the average share of these years in the total costs of other multilateral donors (52.0%).

3. The "preferred creditor" share of El Salvador's public debt service is expected to surpass 60% in the late 1990s, with the World Bank's share exceeding the 20% guideline (World Bank, 1993b, p. 20). Bilateral donors occasionally write off their loans, as when the US forgave $464 million in Salvadoran debt in 1992. In the wake of the 1980s debt crisis, commercial bank loan sometimes have also been, in effect, partially written off (for example, through buy-backs at a discount). Loans from IFIs, however, remain sacrosanct.

4. For discussions of the net transfer cycle, see Griffin (1978, Ch. 3) and Reisen and von Trotsenburg (1988). A recent study for the IDB forecasts negative net transfers from Latin America as a whole to the IDB, perhaps "at quite a high level," by the end of the decade and into the new millennium (Griffith-Jones *et al.*, 1993, p. 77).

5. Since the data in Tables 1 and 2 do not cover exactly the same time periods, it is not possible to measure precisely non-Peace Accord external assistance simply by subtracting the latter from the former. It appears, however, that more than half of external assistance to El Salvador in the postwar years has been earmarked for purposes other than programs mandated by the Accords.

6. Official development assistance from OECD members peaked in real terms in 1990, at $55.6 billion (World Bank, 1994b, p. 196).

7. Total US economic assistance to Central America fell from $824 million in FY 1991 to $462 million in FY 1993 and to $268 million in FY 1994. The decline is even sharper if dated from the peak of FY 1990, when US economic assistance reached $1.3 billion. These figures include development assistance, Economic Support Fund, and PL 480 food aid. (Data supplied by USAID.)

8. During 1980–89, El Salvador received $3.6 billion in US aid. The second largest recipient of US aid in Latin America was Honduras with $1.6 billion (Kan, 1993, p. 44).

9. In 1991 the net disbursement of official development assistance to El Salvador was US$55 per capita, equivalent to 4.9% of GNP; the comparable figures for middle-income countries as a whole were $16 and 0.7% (World Bank, 1994b, p. 198).

10. For discussion, see Mosley (1985).

11. During 1980–91, the US provided $1.8 billion to El Salvador under the ESF (data provided by USAID). The dollars were deposited at the Central Bank, which sold them to importers for colones; an equivalent amount, in colones, was then placed by the Central Bank in a counterpart fund jointly programmed by the government and the United States. Similarly, local currency from sales of PL480 food generated counterparts funds.

12. The loan document notes that "although pledged donor support for the NRP has been generous, much of it has been in the form of slow-disbursing project financing, and most of it has not been directed toward the areas of highest political priority such as training and equipping the new national police, facilitating land transfers, etc." In response to this problem, the government is said to be "intensifying its outreach to the donor community and is making efforts to obtain more balance of payments support, the local currency counterpart of which can be used to finance NRP expenditures" (World Bank, 1993b, p. 5).

13. The ability of NGOs to provide an alternative vehicle for large-scale reconstruction programs was limited by their lack of experience in such activities and by procedural requirements of the donors. For example, USAID became more willing over time to channel limited resources through opposition-linked NGOs, but the agency's ability to do so was constrained by its own bureaucratic rules and procedures. For a discussion of the role of the NGOs, see Washington Office on Latin America (1993).

14. The term "conditionality" here refers to informal policy dialogue as well as formal performance criteria. For a review of recent practice, see Nelson and Eglinton (1992, 1993).

15. El Salvador's agreements with the IMF in recent years have been "precautionary": the country has not actually drawn on the IMF resources available under the stand-by arrangements. The government sought IMF agreements for two reasons: (a) for technical advice on the relationships between policy instruments and macroeconomic objectives, and (b) for the "catalytic effects" that Fund cooperation gives to relations with other creditors. For the latter reason, IMF conditions carry considerable weight even in the absence of actual drawings on IMF resources.

16. The curve drawn in Figure 1 is backward-bending, to allow for the possibility that beyond some point (beyond point A) the net effect of increased government budget deficits may be to fuel social tensions, for example, by sparking hyperinflation.

17. At the April 1993 CG meeting, the World Bank representative reiterated that "adequate external financial support to finance priority peace-related expenditures is the critical condition for the consolidation of peace and social progress within a framework of macroeconomic stability and sustainable growth" (World Bank, 1993a, Annex IV(a), p. 6).

18. Different sources provide conflicting data on defense expenditures. Compared to the IMF data reported in Table 4, government budget data generally show somewhat lower defense expenditures and somewhat higher education and health expenditures.

19. The problem of excess military spending is not confined to El Salvador. Data compiled by the Stockholm International Peace Research Institute indicate great variation among countries in the region in the percentage of GDP devoted to military expenditure (see Table A1).The SIPRI data generally exclude foreign aid-financed expenditures, and hence indicate the "domestic opportunity cost of government appropriations to the military" (Hewitt, 1991, p. 22).

20. The government's November 1991 Letter of Intent included a commitment to reduce military spending from 22% of recurrent expenditure in 1991 to 20% in 1992 (IMF, 1991a, p. 58). This provision does not appear to reflect an IMF initiative, however.

21. Similar objections were raised by the Executive Board of the World Bank when SALs were first proposed in 1980:

> 'The Board did *not* want to use loans to "buy" policy change, to persuade reluctant developing countries to undertake reforms, to induce waverers to do what they feared would be politically painful or to strengthen the hands of reforming groups in developing countries at the expense of their opponents. Using loans as leverage in this way was meddling in developing countries' internal politics; it would damage the Bank's stance of political neutrality and, to be successful, it would require political skills which the Bank did not possess' (Mosley, Harrigan, and Toye, 1991, pp. 35–36).

As in the case of SALs, it is conceivable that current objections to Bank involvement in military expenditure reductions and other "governance" issues will prove transitory.

22. The United States had been the principal financier of the Salvadoran military during the war, providing over $1 billion of military assistance during the 1980s, (Congressional Research Service, 1989, p. 26). This figure includes only direct support via the Military Assistance Program, Foreign Military Sales Program, and International Military Education and Training Program.

23. For reviews, see Ball (1992) and Kan (1993).

24. Conable (1991). Conable cautioned against using rigid formulas for determining where military spending is excessive, but he cited governments which spend more on the military than on health and education combined as an indicator. That year the Government of El Salvador spent 1.26 billion colones on defense and 1.12 billion on health and education (IMF, 1994, pp. 26, 44).

25. IMF (1991b), cited by Polak (1991, p. 52).

26. Quoted by Ball (1993, p. 2).

27. These include Hewitt (1991), Bayoumi, Hewitt, and Schiff (1993), and Happe and Wakeman-Linn (1994).

28. The proposed IDB loan for strengthening the Salvadoran judicial system, mentioned above, is a noteworthy exception.

29. The latter quote appears in a May 1994 USAID memorandum titled "Land: The impossible dream."

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APPENDIX

Table A1. *Percentage of GDP devoted to military expenditure (averages, 1988–90)*

Country	Percentage GDP
Guatemala	1.4
Costa Rica	0.4
Mexico	0.3
Honduras	4.0
El Salvador	3.4
Panama	2.5

Calculated from data presented by Happe and Wakeman-Linn (1994, Table 3). For Honduras, the SIPRI figures are anomalously high (9.6% of GDP); the lower estimate reported here is based on United States Arms Control and Disarmament Agency data for 1988–89.