New Policies for a Changing Global Environment

The Role of the Multilateral Development Banks in Emerging Market Economies

Findings of the Commission on the Role of the MDBs in Emerging Markets

José Angel Gurria and Paul Volcker, Cochairmen

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Commission on the Role of the MDBs in Emerging Markets

This report focuses on the role of the World Bank and other multilateral development banks (MDBs) in the emerging market economies – the 20 or so countries of Latin America and East Asia, plus China, India and Russia, with access to foreign private capital. It addresses two central questions: Should the MDBs continue to lend to this group of countries or, instead, concentrate attention on poorer countries with little such access? Second, what purposes should this lending serve and under what conditions should it take place?

A 30-person Commission chaired by Jose Angel Gurria and Paul Volcker met on two occasions to discuss these questions. The report was prepared on the basis of those discussions and of extensive comments by Commission members on earlier drafts. Commission members listed on page 20 have endorsed the report, though not all necessarily agree with every statement and recommendation.

Preparation of the report was led by Nancy Birdsall (Senior Associate, Carnegie Endowment for International Peace) with Brian Deese (Junior Fellow, CEIP), with the collaboration of Shahid Javed Burki (CEO, EMP Financial Advisors) and Peter Hakim (President, Inter-American Dialogue), and of Joseph Savitsky (EMP) and Rachel Menezes (IAD). The sponsoring institutions would like to thank the Ford Foundation for helping to support this project.

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Executive Summary

Continued Lending to Emerging Market Economies Makes Sense

The MDBs should continue to lend to the emerging market economies as an integral part of their ongoing role in the years ahead.

- Given the immaturity of their economic and financial institutions, the small size and vulnerability of their markets, and the volatility of global financial markets, access of these countries to private capital can be unreliable, limited and costly for them, exposing them to great insecurity even when their long-run growth prospects are strong.

  - Loans from MDBs can encourage public investments with high social and economic returns – investments in education, health, rural infrastructure, bank regulation, judicial reform, and other areas. These are the investments that, by supporting equitable growth in open market systems, crowd in productive private investment.

  - In addition, MDB lending can assist EMEs to cope with the insecurity that stems from volatile capital markets. Since crises tend to hurt the poor most, through lost jobs and income and interrupted education for children, assisting countries to cope with crises helps alleviate poverty and constitutes development lending.

- Lending is a vehicle for policy change and promoting international goals. Services that are bundled with lending also help to support objectives of the global community: poverty reduction, human development, protection of the environment, financial accountability, and standards of public procurement that curtail corruption and promote competition.

- For the non-borrowing member countries of the MDBs, the benefits of MDB lending to EMEs are substantial and they are not costly to taxpayers.

- Lending to emerging markets does not crowd out, but rather indirectly supports, lending to poorer countries.

Longstanding MDB Approaches Toward the EMEs Should Change

At the same time, the Commission believes the MDBs should move more aggressively to adapt to the changing needs of the emerging market economies and to ensure that their lending in those countries advances such agreed international objectives as poverty reduction and increased living standards for all.

- Graduation should be voluntary, but coupled with incentives to avoid prolonged dependence.

- The MDBs should increase further the incentive to graduate by differentiating their pricing according to borrowers' per-capita income in a simple and predictable manner. All the MDBs should develop systematic policies for pricing advisory services.

- The credibility and effectiveness of lending as a vehicle for policy change needs to be enhanced.

  - MDBs should simplify policy conditionality, focus it more consistently on equity as well as growth issues, and desist from lending in the first place when a borrower is not committed to the policy change it is promising. Once conditions are agreed upon the MDBs should be prepared to halt disbursements if governments fail to honor commitments.

  - To support a sustained reform process, policy conditions under discussion should normally be open to public debate. Once conditions are agreed and a loan is approved, the relevant documents should be fully available to the public.

  - Shareholders should also create a mechanism for independent, third-party evaluation of the effectiveness of MDB programs, and whether such programs (including lending and accompanying advice and technical assistance) encourage adequate norm setting, increased attention to poverty reduction, and better policies and stronger institutions generally.

- The MDBs should be ready to lend to emerging economies during times of market and economic crisis, but should do so in a manner consistent with the design and consolidation of medium-term development programs.

- The MDBs should rationalize and strengthen their relationships with the private sector.

  - Shareholders should endorse an expansion of MDB lending to the private sector and other non-sovereigns, in all cases in a manner that catalyzes rather than substitutes for, private lending.

Introduction

The World Bank was founded in the aftermath of World War II to transfer investment capital from capital-rich to capital-poor countries. The initial idea was simple, brilliant, and perfectly adapted to the opportunities and constraints of the immediate postwar period. With private capital flows restricted as well as financially risky, many countries were unable to attract foreign private capital to finance socially productive investments. The solution was to create an institution backed by the capital commitments of the United States and other capital-rich nations that could borrow at the lowest market rates and lend economically to those with urgent needs, first nations ravaged by war and later those in the early stages of economic development. Four regional development banks were founded on the same principle: the Inter-American Development Bank (1959); the African Development Bank (1964); the Asian Development Bank (1966) and the European Bank for Reconstruction and Development (1991).[1]

Throughout much of the postwar period, the capital structure, financing policies, and administrative arrangements of the World Bank and the regional banks (together the multilateral development banks or MDBs) were defined largely by that original mission. They lent to finance government-led investments, mostly in transportation, power and other infrastructure projects. Over time, the member governments of the banks endorsed additional mandates. In the 1980s, the banks began lending to support the opening of economies and their structural adjustment to the global market. By the 1990's they had assumed a major role in the battle against poverty in developing economies.[2] Earlier, the MDBs worked to reduce poverty through highly concessional lending to the world's poorest countries, mostly in Africa and South Asia. These loans were financed, not by MDB borrowing, but through the direct contributions of rich countries to subsidized "soft money" windows of the MDBs. Over time, the regular loans of the banks gave an increasing emphasis to supporting policies and programs to reduce poverty and strengthen health, education, and other programs of human development, including in the emerging market economies.

In the 1990s, private capital flows to many middle-income countries, and to a few low-income countries such as China and India, increased dramatically. Private flows to some countries suddenly outstripped – by wide margins – the flows from the MDBs (see Annex Section 1, Table 1), raising the question whether the original mission of the MDBs still made sense in those economies. At almost the same time, critics claimed that MDB lending had not been effective at reducing poverty. Other concerns about the MDBs were also accumulating: neglect of the environmental costs of projects; lack of coordination with each other, with bilateral donors, and the IMF; lack of transparency; excessive and ineffective conditionality; and neglect of their responsibility for the enormous accumulation of official debt without growth in the world's poorest countries (see Annex Section 2).

Concurrently, the rich donor governments increased further their demands on the World Bank and the regional banks. The MDBs were urged to provide advice and lending to a large number of new countries following the fall of the Soviet Union, and to deal with debt management, financial crises, corruption in borrowing countries, donor coordination, and the provision, through special grants, of such global public goods (GPGs) as protection of biodiversity. The increasing demands raised the cost of doing business, and have helped keep staff and administrative budgets high in relation to lending volume. (See Section 2 of Annex).

As with democracy (recalling Churchill's point), the relevant parties, though obviously unhappy with the banks, would be even unhappier without them. The banks' owners, i.e. their member governments, have not identified any better institutional alternatives for managing the growing number of international finance and development tasks.

Growing demands, rising costs, and worries about effectiveness raise real questions about priorities, both for government members who ultimately set program priorities, and for the management of the banks who are responsible for program implementation and effectiveness. This report focuses on one of the issues raised, an issue that is fundamental for the government shareholders: the appropriate role, if any, of the MDBs in emerging market economies (EMEs), defined as those economies with good access to private capital markets. (See Section 1 of Annex for our definition of EMEs and the countries included in that definition). It addresses two specific questions:

- In light of the needs of the poorest countries (e.g. the HIV/AIDS and debt problems of Africa), should the MDBs continue lending to the emerging market economies?

- If they should, what purposes should that lending serve and under what conditions should it take place?

The Commission believes that the answer to the first of these questions is yes. **The MDBs should continue to lend to the emerging market economies as an integral part of their ongoing role in the years ahead.** Though lending should not go on indefinitely in every individual country, there is no need for an arbitrary or predetermined deadline.

At the same time, the Commission believes the MDBs should move more aggressively to adapt to the changing needs of the emerging market economies and to ensure that their lending in those countries advances such agreed international objectives as poverty reduction and increased living standards for all. The MDBs can enhance their approach toward the EMEs in specific ways that are consistent with sustaining a reasonable level of lending and MDB income, taking into account that the volume of lending to the present group of emerging markets is likely to decline over time.

The Commission members addressed the two questions with the objective of defining recommendations for the shareholder governments. The recommendations do not necessarily or adequately cover questions of internal management.

I. Continued Lending to Emerging Market Economies Makes Sense

The MDBs should continue lending to the EMEs for four reasons.

1) **Given the immaturity of their economic and financial institutions, the small size and vulnerability of their markets, and the volatility of global financial markets, access of these countries to private capital can be unreliable, limited and costly for them, exposing them to great insecurity even when their long-run growth prospects are strong.**

Access to global markets for debt and equity can provide support for the growth of emerging market economies and can help them deal with deep-seated problems of poverty. Yet, in emerging market economies, creditors and investors, both domestic and foreign, face uncertainty about macroeconomic stability, financial sector depth and regulatory capacity, and political risks. This is the case even in countries that have reduced inflation and dramatically deregulated and opened their markets.

Only time and performance – much more than a decade of steady, sound economic policies – and visible resilience of economic and political institutions, will induce domestic and foreign creditors and investors to accept lower returns for their capital in return for lower country risk.

In the meantime, longer-term and cheaper loans from MDBs can encourage public investments with high social and economic returns – investments in education, health, rural infrastructure, bank regulation, judicial reform, and other areas – that do not yield commercial returns to private agents, and which otherwise might not find a place in national budgets. These are the investments that, by supporting equitable growth in open market systems, create an environment that crowds in productive private investment.[3]

In addition, MDB lending can assist EMEs to cope with the insecurity that stems from volatile capital markets. Experience provides ample evidence that the cost and availability of funds in international markets can change abruptly, sometimes for reasons beyond the control of any particular country. In the process, growth, development plans and poverty programs may be severely impaired. When global turmoil partially or completely closes market access, multilateral lending can assist in sustaining adequate public spending on education and health, restructuring and strengthening regulatory and supervisory capacity, and developing social safety nets. **Since crises tend to hurt the poor most, through lost jobs and income and interrupted education for children, assisting countries to cope with crises helps alleviate poverty and constitutes development lending.** (See Box 1). Moreover, when the MDBs maintain and even increase lending during periods of stress, they signal their support for responsible development policies[4], and with relatively modest amounts, may help rebuild market confidence.

Box 1: Mexico 1995 – Emergency lending for medium-term development

With the financial crisis triggered at the end of 1994, GDP per capita in Mexico contracted 8.2% in real terms in 1995 and open unemployment rose to 7.3% (from 3.7% in 1994). To avoid a high fiscal deficit, the government increased substantially the prices charged by public enterprises, raised the value-added tax rate (from 10 to 15%), and reduced expenditures. Budget tightening and increased debt servicing meant a substantial cut in social spending (education and health/labor spending contracted by 9.7% and 11.6% respectively in real terms).

In the context of these budget cuts, the World Bank and the IDB approved loans totaling $ 3 billion for Mexico ($1.5 billion each). $ 2 billion went to support the restructuring of the country's financial system, a critical step in restoring market confidence. $1 billion went to help preserve essential social services for the poor during the crisis, and support their restructuring to make them more efficient and fiscally sustainable. The quick-disbursing loans were thus tied to politically difficult bank restructuring and to agreements on maintenance and strengthening of the most efficient social programs. The financial sector loans helped the government implement comprehensive, medium-term reforms to increase the soundness and transparency of the financial sector. Among the reform measures supported were evaluation of the banking system, re-structuring of problem banks, reforming accounting standards, and improving the sector's regulatory framework. The social loans helped minimize the losses in human capital that financial crises often trigger in developing countries, including child malnutrition and children leaving school to go to work.

2) Lending is a vehicle for policy change and for promoting international goals and standards.

Political and social constraints in emerging markets, as well as technical complications, make it difficult to design and implement many reforms – of health, banking systems, bankruptcy law, unemployment programs, etc. Officials from countries such as Brazil, Mexico, Turkey, Hungary, Thailand, and Korea repeatedly cite the services that are 'bundled' with MDB financing as a key reason for seeking MDB loans. They value the detailed, project, and sectoral and economic analysis of MDB staff and the dialogue on tough internal policy and budget choices that the lending process catalyzes.

These services that are bundled with lending also help to support objectives of the global community: poverty reduction, human development, protection of the environment, financial accountability, and standards of public procurement that curtail corruption and promote competition.[5] Even if the financing for a MDB-supported project is supporting other government expenditure (because money is fungible, see Box 2), the technical and advisory services are specific to the program or policy being supported. The recent emphasis of the MDBs on governance issues – accountability of government, and adequate representation of all citizens in economic decision-making – can also contribute to the strengthening of democratic systems in emerging market economies.

Most borrowing member countries work with at least two of the MDBs: the World Bank and the relevant regional development bank. The banks work within the same overall policy framework set by shareholders (all for example in recent years making poverty reduction the explicit priority and increasing lending for social programs). Within that framework, the banks can improve coordination – and reduce their and borrower costs by for example harmonizing procurement standards and sharing environmental assessments.[6]

Box 2: Fungibility of Money and MDB Bundling of Financing and Advice

Money is fungible, and MDB lending for education and rural roads could end up allowing governments to shift their own resources to less desirable spending that the MDB might not have endorsed. For this reason, MDB lending must be linked to borrower commitments to sound policies and overall sound use of their own resources. The MDBs can ensure such a link because they have an enforcement mechanism not available to the private sector – the promise of future financing at below-market rates. They can also formalize understandings about borrower commitments, either by lending only when such commitments have already been translated into visible, policy steps, or by conditioning disbursements on agreed future steps. Furthermore, MDB lending usually constitutes a so-called "bundle" -- of financing plus technical and advisory services. Thus even when the financing, for a health project for example, is fully fungible, the policy dialogue on allocation of public resources to health, and technical input on reform of health insurance or hospital administration, is not.

At times, MDB lending may "finance" a desirable program without adding to total government spending. This makes sense; many developing countries, including most emerging market economies benefiting from private capital inflows, are implementing concerted programs of fiscal discipline. Where that is the case, the MDBs are both supporting the specific program (health reform for example) and helping diversify the "credit mix" available to emerging markets as they cope with managing their overall foreign liabilities and their current account. For countries trying to limit the amount and control the timing of their recourse to the markets, even relatively small amounts of financing from the MDBs for programs of high priority can thus provide critical help.

The provision of some non-lending services can be separated from lending, and some governments have paid directly for advice from the MDBs without borrowing. However as a practical matter, the advice is taken more seriously, and is more likely to be effectively enforced if backed by and tied to a loan. The process of negotiating the loan and the borrower's associated commitments to reform generates better information for both parties on feasible policies and institutional capabilities. And the loan commitment gives the MDB itself a greater stake in rigorous analysis and enforcement.[7]

3) For the non-borrowing member countries of the MDBs, the benefits of MDB lending to EMEs are substantial and are not costly to taxpayers.

In an increasingly interdependent global economy, the U.S. and other non-borrowing members of the MDBs have a substantial stake in the policy choices and institutional resilience of the emerging market economies. Their financial stability contributes to global financial stability. Their social and economic decisions affect the health and well-being of their own peoples, undermining or advancing such global goals as poverty reduction. And their decisions – on energy use, food safety, efforts to reduce drug trafficking and corruption and so on – increasingly affect the once-insulated residents of rich countries.

Meanwhile, the cost to the U.S. and other non-borrowers associated with MDB lending to the EMEs is surprisingly small. The annual cost of direct new contributions is tiny. In the case of the U.S. and the World Bank it is zero; no new appropriations are needed to support regular World Bank operations.[8] There is an opportunity cost of the capital of non-borrowers held in the MDBs, and non-borrowers face the risk – remote as it is – that their guarantee to cover unmet debts of the banks could be called. These costs are difficult to measure. We estimate the

annual opportunity cost of the capital of the U.S. in the World Bank to be about $375 million. (Box 3). The cost of a call on the callable capital could be higher, however in more than 50 years, there has never been such a call by the World Bank or any of the other MDBs.

Box 3: The opportunity cost for US taxpayers of capital ownership in the World Bank*

The capital shares of member governments in the MDBs consist of a paid-in and a callable portion. In the case of the U.S. capital in the World Bank, about $2 billion is paid in and about $30 billion is subject to call in the extremely unlikely event of a Bank default on its own bonds. Multiplying the $2.1 billion of paid-in capital by 7% (the figure the Meltzer Commission used to represent the annual long-term cost of capital) yields an annual opportunity cost (the lost opportunity to use that capital elsewhere to generate that return), to U.S. taxpayers of about $150 million. There is also an opportunity cost of retained earnings. The annual "dividends" for the U.S. on its portion (17%) of annual retained earnings of about $3.2 billion would be about $225 million. The annual cost of the callable capital is more difficult to assess. It is a function of the risk that some or all of it would in fact be called in a particular year. In 50 years, that has never happened. Indeed the MDBs' financial policies are highly conservative in order to virtually eliminate that possibility. Even a tiny risk – say of .01 % – implies an outlay of some portion of $3 billion (the portion depending on the size of the call and the outlays of the other members). On the other hand, each year that the capital is not called, the annual cost is zero.

The total cost to U.S. taxpayers of membership in the World Bank is thus between $375 million, a small amount (in the light of the benefits outlined in this report), and, were there a call on its capital, up to some billions of dollars.

*This calculation does not include the highly concessional "soft" window, IDA, which does not lend to the EMEs.

4) Lending to emerging markets does not crowd out, but rather indirectly supports, lending to poorer countries.

Commission members also noted that lending to EMEs does not crowd out lending to poorer countries. The MDBs (possibly excluding the ADB) have a sufficient capital base and thus more than adequate 'head room' to finance operations in both the EMEs and poorer countries. Greater lending to countries without the kind of access to private markets of the EMEs – Egypt, Jamaica, Jordan, Morocco, Bulgaria, Guatemala, Paraguay, and others – is constrained by absorptive capacity or policy shortcomings, not by insufficient MDB capital. Loans to the EMEs should not in any event be considered one-for-one substitutes. Diversification reduces overall portfolio risk, stretching to some degree the amount of lending to the poor that can be supported by a given capital base. A portfolio concentrated only in the poor countries would be much riskier, requiring more capital per unit of lending.

To the extent the poorest countries borrow from the highly concessional "soft" windows of the MDBs (IDA at the World Bank), there is no opportunity cost because their borrowing is financed by periodic, separate contributions, primarily by the bilateral donors, not by the MDBs' own borrowing on international capital markets.[9] Indeed in the case of the World Bank and the ADB, net income ("profits") derived in part from lending to EMEs has been periodically transferred to their soft windows, so lending to EMEs has indirectly helped to support the highly concessional lending to the poorest countries.

Finally, in a world that is increasingly interdependent, MDB support to the EMEs may also indirectly benefit their

poorer neighbors. A healthy Brazil not only reduces the risk of financial contagion that could be costly for Argentina and Russia, but also provides a stable growing market for Ecuador and Bolivia. Similarly growth in Korea and Malaysia is likely to benefit Viet Nam.

II. Longstanding MDB Approaches Toward the EMEs Should Change

While the Commission supports continued lending to the EMEs, it also recommends changes in longstanding practices of the banks toward these countries. New approaches in four areas are discussed below: Pricing, especially as an aspect of graduation policy; conditionality and transparency in EME lending and their links to standard setting and policy change; management of emergency situations consistent with MDBs' development objectives; and the MDBs' relationship with the private sector.

1) Graduation should be voluntary, but coupled with incentives to avoid prolonged dependence.

While Commission members agree that as countries grow richer and gain more stable access to international capital markets they should borrow less from the MDBs and eventually cease borrowing altogether, they believe the process should be voluntary.[10] A voluntary graduation policy, coupled with incentives, gives the MDBs the flexibility to deal with individual countries' needs, and reflects the fact that countries tend to "self-graduate" on their own accord (Annex, Table 9).[11] Incentives built into the cost and design of borrowing can help avoid prolonged dependence and encourage countries to manage their own finances to achieve and maintain access to private capital.

MDB public sector loans are currently priced in a uniform manner known as "cooperative pricing", i.e. all government borrowers face the same interest costs (though the rate varies over time and across banks) for virtually all loans.[12] With cooperative pricing, emerging market economies already have an incentive to reduce or stop borrowing when their own credit rating improves, since a lower cost of private capital reduces the spread between the cost of MDB and private market credit. The declining spread, combined with preparation and negotiation tasks involved in MDB loans and the delays MDB borrowing entails, explains the voluntary "graduation" of Korea and Malaysia in the early 1990s (until the 1998-1999 crisis), and the greatly reduced borrowing of Hungary, Poland, and Chile.[13]

The MDBs should increase further the incentive to graduate by differentiating their pricing according to borrowers' per-capita income, in a simple and predictable manner.

Charging higher income countries higher rates has been criticized for seeming to penalize success on the grounds that commercial banks normally charge more creditworthy borrowers less rather than more. But the MDBs, unlike commercial banks, are charging below-market rates to start with, passing on the benefit of the guarantees of the non-borrowing members against their liabilities. Rates that rise with per capita income would simply reduce that benefit as borrowers grew richer. For borrowers also benefiting from falling spreads in the market, the subsidy would decline in pincer-like form, with their MDB rates rising and their differential with market rates falling. The result would be to bring MDB rates closer to the market faster. Pricing tied to per capita income rather than to the sovereign credit rating

has the additional advantage of ensuring that relatively poor countries that achieve high credit ratings (such as Botswana, El Salvador, and China) are not penalized for their success.

Differential pricing should be kept simple and predictable, with, for example, two to three step-ups from current rates.[14] Rates should be announced, set, and non-discretionary. To the extent higher (though still below-market) rates were to reduce demand for borrowing, self-graduation would be accelerated. To the extent borrowers continued to see benefits in the bundling of policy dialogue and technical assistance with the below-market cost of borrowing, the banks would generate more income from loans.[15]

Obviously middle-income borrowers would prefer to avoid higher rates, and defining such a policy would be controversial. An increase in borrowing costs for some countries would have to be built on support from the EMEs and on the understanding that they should play a larger role in setting priorities for the use of any extra income, and in general in the MDBs' decisions. They would have to have a central role in the consultations and analysis that lead to new proposals.

In the past, a portion of net income has been allocated by shareholders for special purpose grants (see Box 4), including for "global" programs such as CGIAR and the Global Environment Facility. In the future, higher income could help fund newly pressing needs such as tropical disease research and control of such global risks as mad cow and foot-and-mouth disease. This would require agreement of all shareholders; the large borrowers, including the emerging market economies, would reasonably want appropriate input in setting the agenda for the allocation of net income, and would no doubt insist on donor country contributions to supplement transfers from net income to support these global initiatives.[16]

Box 4: The MDBs' Sources and Uses of Income

The MDBs generate income from two major sources. First, their paid-in capital and retained earnings are invested in interest-earning assets, especially in loans to their members. The paid-in capital and retained earnings are sometimes called "free funds" because the MDBs do not have to pay interest or fees when they utilize those funds; as a result the net return they receive from investing these funds is the same as the full amount of the interest earned on the assets. Second, the MDBs borrow on world capital markets and use those funds to support additional assets -- loans and liquid assets. On those borrowed funds, the MDBs earn a net interest spread. In the case of the IBRD (the hard-loan window of the World Bank Group) in fiscal year 2000, these two sources amounted to about $1.8 billion and $800 million, respectively, with the bulk of the latter amount (attributable to the net interest spread) due to the spread on loans. A portion of this income is used to cover administrative costs (about $900 million) and credit loss provisions and to maintain adequate reserves. Another portion is allocated, by agreement among shareholders, to special activities. In fiscal year 2000 the World Bank provided about $125 million in grants through its Development Grant Facility, including for example for agricultural research through CIGAR. In addition, from fiscal year 2000 net income, shareholders of the World Bank allocated about $350 million to the Bank's highly concessional lending window for the poorest countries, IDA, $250 million for debt reduction in the poorest countries (the Highly Indebted Poor Country Initiative, or HIPC), $30 million for capacity-building in Africa and $35 million to a trust fund for Kosovo.

Similarly, in the regional development banks, the EMEs might want to use income transfers to finance grants for the promotion of programs of regional interest. Coordinated regional interventions could minimize the spread of diseases and pollutants by air and

water from one country to another. Regional institutions could be established to finance investments in countries with small populations or small economies. Promoting regional infrastructure projects – road, water, rail, and telecommunications – also falls into this category. Grants funded by income could complement investments underwritten by the large countries in a region.

As emerging markets reach the point of self-graduation, some may want to continue to benefit from the non-lending services of the World Bank and their relevant regional bank. Former borrowers and countries that are now reducing their borrowing substantially have in the past paid directly for non-lending services from the World Bank (see Annex Section VII on Saudi Arabia and Chile). But pricing of these advisory services has been *ad hoc*, negotiated on a case by case basis, and (as far as we can ascertain) done only by the World Bank. **All the banks should develop systematic policies for pricing advisory services** – to not only cover real costs but to minimize any implicit cross-subsidy from lower-income countries that are borrowing, and to minimize any risk of creating unfair competition for privately provided consulting services. Such a policy would accommodate countries moving toward self-graduation, while supporting a continued policy role for MDBs that would be demand-driven.

The MDBs have already taken initial steps in the direction of charging different rates for different loan products by charging higher rates for the large and quick-disbursing emergency loans to Korea, Brazil, and Argentina in 1998. There are additional possibilities. Linking non-interest rate charges (commitment and other fees) to administrative costs would give increasingly capable EME borrowers an incentive to anticipate and build much more of the necessary policy reform, engineering design, environmental safeguards, etc. into loan requests. This would reduce delays and increase both the ownership of programs and the effectiveness of their implementation. Allowing borrowers a greater range in the maturity of loans (though still for not less than 10 years) would increase borrowers' options and encourage more active overall management of both their public and private debt.

2) The credibility and effectiveness of lending as a vehicle for policy change needs to be enhanced.

Commission members ground their support for continued MDB lending to the EMEs in the role that such lending can play in encouraging good economic management, investment in institution-building, and policies that reduce poverty and inequity. The institutions have mechanisms to link lending to these kinds of changes. The "enforcement" mechanism of future access to MDB loans is one. It requires that MDBs stop lending when governments fail to honor their commitments. A second is conditionality, which ties disbursements of loans to agreed-upon policy changes by governments.

Conditionality has invoked criticism from all sides. Some invoke evidence that the policies of the "Washington Consensus" supported by the MDBs have not been associated with growth[17] and have ended up hurting the poor. Others criticize conditions that call for more

taxes or higher expenditure, and assert that conditionality has undermined sovereignty and democracy. Some World Bank economists, focusing on Africa, say conditionality weakens country "ownership" of reforms, and is thus ineffectual. They and others call for an approach to conditionality that reflects greater humility by MDBs *ex ante* about what works and more flexibility *ex post*, as programs are implemented.[18] And the argument that conditionality only works *ex post*, i.e., as a reward for already demonstrated good performance, is currently gaining ascendancy.

(These criticisms of conditionality have focused on the policy conditions in large adjustment loans that disburse relatively quickly and provide budget support.[19] There are also conditions or triggers in investment or project loans, e.g. that new roads will be financed only when a budget commitment to maintain existing roads is made. Conditions are also associated with the standard fiduciary obligations of the MDB lenders, including on accounting and auditing and increasingly regarding environmental and other safeguards. These types of conditions have been less controversial.)

Commission members are aware of the problems with policy conditionality. In some cases, where governments have already undertaken change on their own, big lending programs can proceed without conditionality. But there are instances where a government needs financial support to begin a reform process. In these cases, the challenge is to ensure that conditionality focuses on the fundamental issues of growth that reduces poverty;[20] that the programs and policies incorporated in the lending conditions are home grown, reflecting real borrower commitment; and that the process is made credible by sensible enforcement.

To ensure that conditionality augments rather than undermines the effectiveness of MDB lending, the **MDBs should simplify policy conditionality, focus it more consistently on equity as well as growth issues, and desist from lending in the first place when a borrower is not committed to the policy change it is promising. Once conditions are agreed upon the MDBs should be prepared to halt disbursements if governments fail to honor commitments.**

Where policy reform is in fact owned by, rather than forced upon, governments, and where it reflects a reasonable level of understanding by all parts of government and indeed by citizens and thus is politically viable, it can in fact be a useful instrument for the borrower.[21] It can be helpful in advancing politically difficult reforms – for example due to resistance from a local private elite – that are necessary for long-run, equitable growth. Conditionality cannot substitute for borrower commitment, but assuming that commitment is there – by governments that are accountable to their citizens – conditionality can also help governments signal to local and foreign investors their readiness and political ability to sustain the reform program. This has been the case in many of today's emerging market economies in Latin America.

The MDBs are trying to simplify policy conditionality, and reduce the number of conditions so they are manageable and reflect high priorities. Current World Bank adjustment loans have far fewer tranche release conditions than in the late

1980s, when dozens of conditions were not uncommon.

But the issue is also design and focus of conditionality, to include policies to protect the poor, and its credible enforcement, including by halting lending.[22]

Enforcing conditionality may mean that lending will be much more selective across countries.[23] Big lending programs will be confined to countries that are committed to equitable growth and have the institutional capacity and the public support to make them work.[24]

To support a sustained reform process, policy conditions under discussion should normally be open to public debate. Once conditions are agreed and a loan is approved, the relevant documents should be fully available to the public.[25]

Commission members support the argument that conditions ideally flow from an open and participatory debate within countries regarding the overall development agenda as well as the specific loan agreement.[26] The most sensible way to encourage such open debate is to make the process and documentation as transparent as possible.

Shareholders should also create a mechanism for independent, third-party evaluation of the effectiveness of MDB programs, and whether such programs (including lending and accompanying advice and technical assistance) encourage adequate norm setting, increased attention to poverty reduction, and better policies and stronger institutions generally.

A lesson of the last decade is that the MDBs can err in their policy prescriptions. A new approach to conditionality alone will not guarantee greater effectiveness in supporting sustainable and equitable growth. An increase in transparency and a commitment to independent evaluation is also critical. The World Bank (and the IMF) have already sponsored such outside evaluations of adjustment lending, though on an *ad hoc* basis.

A mechanism of outside evaluation would not substitute for the audit and evaluation work which each bank now sponsors by separate units that report directly to the boards. However, coupled with the banks' own assessments, it would enhance the MDBs' capacity to identify sources of waste, inefficiency, and corruption and evaluate the policy advice and effectiveness of programs, including their effects on poverty.

One approach would be for each MDB to develop a system of regular outside reviews. For example, every few years a panel of eminent persons, with experience in government, the private sector, and civil society, would Commission and oversee independent performance audits and evaluations of MDB programs, with a particular focus on the effects of programs on growth and poverty reduction. Their mandate would include but not be limited to review of the banks' own evaluation work.

The results of independent evaluations should be published and open to public scrutiny, ensuring transparency and accountability on the admittedly difficult question of appropriate policy influence.

3) The MDBs should be ready to lend to emerging economies during times of market and economic crisis, but should do so in a manner consistent with the design and consolidation of medium-term development programs.

The MDBs should not be viewed only as an adjunct to emergency IMF stabilization lending programs, and should not be called upon solely to provide loans to round out amounts deemed desirable for "credible" support packages. Emergency lending must be structured so that it supports the kinds of programs referred to above.

The MDBs could also develop a product to provide pre-approved counter-cyclical support to help emerging markets anticipate, respond to, and ultimately avoid financial shocks.[27] With appropriate eligibility and *ex ante* performance standards, the banks would approve financing that countries could easily and quickly draw on in the event of crisis. A drawdown option of this kind[28] makes particular sense in countries that in normal times have good access to private markets, because of a reasonable policy and institutional environment.

4) The MDBs should rationalize and strengthen their relationships with the private sector.

In the last decade, most emerging market economies have dramatically reduced the role of government in the production and the provision of banking and public services, privatizing industrial and commercial enterprises, and issuing concessions for long-term private management of power, water, transport, and other services. In many countries, the gains in efficiency and increased access, especially for poorer households formerly without public services, have been notable.[29] However, countries still face yawning gaps, especially in infrastructure, which private investors and creditors have not come close to filling. A World Bank assessment in the mid-1990s suggested Latin America needs an additional $60 billion in infrastructure investment. The problem is that private lenders and investors are unlikely to finance many otherwise viable projects whose return is vulnerable to government and regulatory risk, i.e. to change in local or national government policies or practices. Indeed, in large infrastructure, profitability is dependent on governments honoring agreements.[30]

As a result there is considerable potential for the MDBs to catalyze privately led project finance – based on their knowledge of the policy and institutional environment, their technical and financial competence in infrastructure, and their ability to help governments commit to appropriate policy because of their interest in maintaining the support of the official financial community.[31]

While each of the MDBs provides lending and guarantees to the private sector and other non-sovereign borrowers (e.g. to municipal, state and local governments) in some form, the overall share of non-sovereign lending as a percentage of total MDB operations is very small (see Box 5 and Table 2). Such lending increases risk for the MDBs since repayments are not guaranteed by a sovereign member. Shareholders have hesitated to assume too much of this added risk on the institutions' balance

sheets. But they have also moved slowly to change the MDB approaches because of the difficulty of overcoming inertia in large, international institutions.

Box 5: MDB private sector lending constraints

In the case of the World Bank, lending without the sovereign guarantee is prohibited by its charter. A separate entity, the IFC, was created by bank shareholders to do only private sector lending. Its current capital base is entirely paid-in, $2.3 billion, compared to the $188 billion of the World Bank, including callable capital (see Table 4). In the IDB, up to 5 % of the outstanding portfolio can be committed for lending to the private sector, over and above what have been small additional amounts to other non-sovereign entities such as the sub-regional development banks. The IDB also has a partner, the IIC, that lends to small and medium enterprises; though often compared to the IFC, its mission is different and its capital base far smaller ($700 million) than that of the IDB itself ($100 billion including its callable capital). To a lesser extent, both the AfDB and the ADB have private sector operations, including the use of equity instruments. In the EBRD, in contrast, about 60% of lending goes to the private sector. The EBRD was founded in 1991 explicitly to help the countries of the former Soviet Union and of Eastern Europe make the transition to market economies. Its capital base is limited ($19 billion), but a high percent is paid in to strengthen its financial base for relatively riskier lending.

However, given the needs of the EMEs, and the increased willingness of private lenders and investors to accept commercial risks if at least some country or political risks are mitigated, **shareholders should endorse an expansion of MDB lending to the private sector and other non-sovereigns, in all cases in a manner that catalyzes rather than substitutes for, private lending.** To ensure public lending does not substitute for private, MDB lending should be restricted to a minority portion of any particular transaction, and the pricing of loans should be market-based.

In the case of the World Bank, shareholders should request a careful assessment of the advantages and disadvantages of such options as increasing the capital of the IFC, allowing the IFC to take a subordinated loan from the World Bank, or endorsing greater emphasis on the IFC selling its own loans in the market, so as to increase its near-term lending capacity.[32] In the IDB and ADB, shareholders should review the possibility of raising the current institutional ceilings on lending without the sovereign guarantee (in the IDB, for example, to above 10%). [33]

The MDBs could also better exploit their ability to issue guarantees to public (and private) entities as a way to catalyze private lending and private investment.[34] MDB guarantees to public entities can be useful in two purposes. The first is to extend loans that are currently available on the market for, say, five years to ten or fifteen years. By guaranteeing the long-term end of loans, the MDBs could help finance projects that have high economic returns but whose long gestation periods make them too costly to finance completely in the market (e.g. infrastructure).[35] The second is to guarantee sovereign and other issues that, with a partial guarantee, bring an issue up to investment grade, allowing access to a much larger pool of institutional investors.

Guarantees are currently valued like loans, usually making them unattractive to borrowing members in comparison. Their increased use is unlikely in the absence of shareholder review of the current financial and pricing policies that limit their appeal.

A development financing model for the 21st century?

For most of the postwar period the World Bank and the regional banks have had two kinds of members, financial backers (non-borrowers) and financial beneficiaries (borrowers). The rules, norms, financial policies, and governance structure of these multilateral membership organizations reflect that simple distinction.

A development financing model for the 21st century could include a 'borrower's club,' where all of the owners (financial backers) are also borrowing members. This is the fundamental logic behind institutions such as the Andean Development Corporation and the Nordic Investment Bank. The Andean Development Bank's owners are all borrowers. With high paid-in capital since 1993, the bank has maintained an investment grade credit rating higher than the rating of any of its sovereign members, despite great volatility in the region (see Box 6). The Nordic Investment Bank is a borrower's club that finances public and private projects, focussing on reducing the cost of trans-border economic interaction.

A multilateral EME financing institution would not substitute for the lending role of the World Bank and the regional institutions as vehicles to promote policy change, institution building, and poverty reduction. But an EME borrowers' club would complement the existing institutions, providing this group of countries, uniquely situated in global capital markets, a mechanism to completely 'own' investments and set their own collective development agenda.

Box 6: The Owners are the Borrowers: the Andean Development Bank

The Andean Development Bank (better known for its Spanish language acronym CAF, Corporación Andina de Fomento) provides development financing to promote sustainable development and integration in the Andean region. It is currently the leading source of multilateral finance in the Andean region, and its capital ownership is structured so that the five sovereign Andean shareholders (Bolivia, Colombia, Ecuador, Peru and, Venezuela) contribute over 95% of the paid-in capital and 99% of the callable capital of the institution. Its owners/shareholders have borrowed nearly $25 billion to date, on terms they would not have enjoyed outside the collective they have formed.

Unlike the World Bank and the large regional banks, the ratio of paid-in to callable capital is high, nearly 50% (compared to about 5% in the IBRD and IDB, and about 35% in the EBRD). The CAF's high paid-in capital along with prudent financial management give it credibility in international markets that exceeds that of any of its individual sovereign members.

In 1993 the CAF received an investment grade rating from Standard & Poor's, Moody's and Fitch rating services. Since 1993, the CAF's rating has continued to improve, and its 'A' rating is now higher than that of any sovereign in Latin America. The strength of its reputation in international capital markets has allowed the CAF to extend its sources of funds and lower its costs of borrowing. CAF's unparalleled success in a region that has been characterized by volatility, economic crisis, and political instability has much to do with its unique set-up. Shareholders have clear self-interest in maintaining and increasing the CAF's institutional credibility, and have opted to keep their obligations to CAF in full despite numerous crises.

Notes

[1] The EBRD from the beginning made loans to the private sector as well. In addition to the World Bank and the large regional banks, another 15 or so multilateral banks operate at the sub-regional level – including the Andean Development Bank, the Central American Development Bank, the European Investment Bank, and the Islamic Development Bank.

[2] The EBRD's major function is to assist countries make the transition to the market, and it has not by its nature been as directly focussed on poverty.

[3] See Annex section 4 on the catalytic role of MDB financing.

[4] As we discuss later, these policies should not be forced upon governments but should reflect country-specific needs and a reasonable level of agreement with government, and a reasonable level of public encouragement and support.

[5] Specific goals covering poverty reduction, universal primary education, gender equality, infant-child and maternal mortality, access to reproductive health services, including HIV-prevention services, and reversing the loss of environmental resources through sustainable development have been agreed to by all nations through the series of global summits from Rio (1992) to Beijing (1995), by the bilateral donor governments in 1996, and by Heads of State at the Millennium Summit of the General Assembly of the United Nations in 2000, and have been adopted by the IMF, the World Bank and the UN development agencies as a framework for their activities and for coordination among them. The fact is that on some of these issues, donors and others apply pressure on the MDBs because, in part, they conclude there are few other more effective instruments for bringing about progress.

[6] Specialization or segmentation of the jurisdiction of each MDB, however, either by sector, by type of project or by type of goods financed risks creating an MDB monopoly. Some competition keeps the MDBs, and their staff on the ground level, well honed and attentive to local programs and policies.

[7] Rodrik 1996 argues that in the absence of lending, MDBs have little monitoring incentive, to ensure that their advice is being followed, and little incentive to exercise their information function as effectively as possible.

[8] This is also true in the IDB. Regular World Bank operations refer to the IBRD, the non-concessional "hard-loan" window of the World Bank Group. The U.S. and other non-borrowers do contribute annually to the concessional IDA window of the World Bank, which does not lend to the EMEs; the contribution of the U.S. to IDA's Twelfth Replenishment (the three-year period from July 1, 1999 to June 30, 2002) is $2.3 billion, or $766.7 million annually. Total annual capital contributions by the U.S. to the other three MDBs are on the order of $55 million.

[9] In the IDB, borrowers also contribute to the soft loan window.

[10] Commission members opposed the idea of setting graduation requirements based on per capita income or sovereign credit rating, as was suggested by the Meltzer Commission. An arbitrary rule can create perverse incentives and prevent lending to countries still in need of MDB financing. Moody's recent upgrade of Botswana'a sovereign debt to investment grade rating, under the Meltzer criteria would exclude a country where 17 % of the population is HIV infected from receiving MDB support.

[11] As the emerging market economies gain access to international capital markets, they tend to reduce the volume of borrowing. Some, including Korea, the Slovak Republic, Hungary and Chile, have prepaid MDB loans and ceased borrowing altogether of their own accord. Countries stop MDB borrowing for various reasons: the lower cost is insufficient to offset the extra time, administrative costs, multiple conditions, reduced flexibility in payment, additional environmental impact hurdles, etc. Countries such as Chile have continued relationships with the World Bank and the relevant regional bank even when actual borrowing has

been small – primarily to warrant continued dialogue – and have paid for advisory services. Others, like Korea, have moved back to borrowing status as a result of economic crisis.

[12] One of several recent exceptions is the higher rate Korea paid to the World Bank and ADB for its borrowing during the 1997-1998 financial crisis.

[13] Chile did not borrow at all from the IDB from 1995-1998, both years inclusive, and accelerated repayment of some older, more expensive loans (see Annex Section VII).

[14] The details of a new pricing scheme would need to be developed with great care. If the net result were that many EMEs ceased borrowing from the MDBs (or ceased during normal times but then came hurtling back in during crises, or shuttled between different MDBs with different pricing policies), the entire purpose could be defeated, weakening the ability of the MDBs to support poorer countries and global priorities more and undermining their financial sustainability.

[15] Or, assuming little or no effect of higher costs on the volume of lending, the banks could aim for neutral effects on their own income from lending by reducing rates for lower-income borrowers.

[16] In the past, middle-income borrowers have resented and in some cases resisted non-borrowers' support for transferring income from loans to the concessional window, to HIPC, and to other special programs.

[17] Goldstein, 2000; Rodrik, 2001.

[18] Within countries, the argument goes, ideas, policies and practices that are imported via international loans cannot substitute for local political will. Participation of citizens of developing countries in the development and monitoring of the economic reform agenda is key to the viability and sustainability of the reforms. In the absence of a politically sustainable domestic commitment, programs financed from outside are simply unlikely to matter. On the problems as seen from the World Bank, see Collier, 2000; and Stiglitz, 1999, who propose a greater focus on "ownership" and "participation" as opposed to "conditions" per se. A 1998 World Bank study came to the conclusion that conditionality did not influence the success or failure of structural lending, (World Bank, 1998, Chapter 2 and Appendix 2). On the mixed performance of fast-disbursing policy-based loans, see Ranis (2000).

[19] These loans, Structural Adjustment Loans (SALs), were initially a response by the multilateral institutions in the mid-seventies to provide balance of payments support to the oil-importing countries so they could pay their bills following a quantum leap in the price of oil. The SAL has become increasingly important in the banks' arsenal of instruments and has in much of the 1990s constituted at least 25% of World Bank and IDB lending. Some of the SAL support has been counter-cyclical – disbursed when private capital pulled out of the countries where private flows had become important.

[20] The Commission members did not discuss, nor try to define, the right content of conditionality. The emphasis of the Commission on lending as a vehicle for advancing internationally agreed goals points to the logic of conditionality that goes beyond such traditional emphases as fiscal discipline and privatization to protection of social safety nets, reform of tax systems to reduce loopholes and evasion that favor the rich, emphasis on worker rights and so on. Birdsall and de la Torre (2001) propose an alternative agenda, emphasizing equity, to that of the so-called Washington Consensus.

[21] In a meeting of the Carnegie Economic Reform Network (October 30, 2000), Boris Federov explained, "The most terrible thing that the World Bank and IMF could do in Russia would be to remove the conditions on which their loans are based." (forthcoming in CERN 2001) The debate on conditionality has been influenced by the failure of aid in Africa. In Latin America in the early 1990s, the Brady package, supported in part by MDB policy loans, seems to have been more effective.

[22] In the poorer countries (not in our set of EMEs), it is likely that lack of enforcement in the past has done more harm, in the form of more debt accumulation, than good. In Africa there is good evidence that conditionality was not much enforced. All the donors continued to lend to countries with high multilateral

debt, in part to ensure countries could service their debt. The MDBs thus lost any leverage they ever had (Birdsall, Claessens and Diwan, 2001).

[23] Regarding enforcement, the MDBs could define a transparent and systematic process of periodic formal warnings that would precede recourse to stopping loan disbursements.

[24] In fact, most EMEs are likely to meet these criteria most of the time – the greatest problems of design and enforcement have been in countries where reform ownership has been less clear and policy and institutional failures are greater. Nonborrowing shareholders also need to reduce pressure to lend to favored constituents and to insert conditions on too many "favorite" issues in every loan.

[25] Currently shareholders of the World Bank are discussing its disclosure policy. Under current policy, The Country Letter of Intent and Board-approved documents for structural adjustment loans are only made available to the public with the agreement of the borrowing government.

[26] It is not clear, however, that the banks have the ability or the mandate to pass judgement on other societies' political processes (see Birdsall, 2000).

[27] In 1999-2000, Mexico obtained implicit commitments from the World Bank and the IDB for about $10 billion in potential future lending, as part of a larger package, amassed in each year, of "blindaje" (armor-plating) against loss of market confidence in the run up to the presidential election. These MDB commitments, though never formalized in Board-approved loans, were an informal example of a product that the banks' could institutionalize.

[28] The Board of the World Bank is considering a management paper proposing this kind of a "deferred drawdown option."

[29] Estache et.al., 2000.

[30] E.g. on rates the private agent can charge for energy, water or (in the case of toll roads) transport services, on access to and cost of government-controlled inputs (in the case of energy); and on reasonable environmental and other standards.

[31] The IDB model provides a workable example. Private sector lending is confined to infrastructure, and the IDB cannot take more than 25 % of the value of a transaction. Limiting MDB involvement in private sector lending to infrastructure is appropriate. It exploits the comparative advantage of the MDBs in reducing country risk from the point of view of the private sponsors associated with their exposure to 'bad' public sector behavior. Infrastructure investments have high initial sunk costs and long gestation periods, and their profitability is threatened if governments change regulations arbitrarily or undo policies or renege on commitments regarding the prices of inputs and outputs. Partial risk guarantees can be provided by the MDBs to private sector sponsors to cover specific non-commercial risks, such as government's reneging on pricing or performance agreements, as well as expropriation and currency inconvertibility. Partial credit guarantees provided by the MDBs can enable sponsors to obtain longer-term or lower cost financing than is otherwise available, ultimately ensuring a more competitive market – be it for energy, transport – and lower prices for developing country consumers.

[32] Some observers recommend that the board members of the IFC, most of whom also sit on the World Bank Board, be chosen to better represent private sector experience.

[33] IDB shareholders are currently reviewing the size of the private sector window based on the work of an External Review Group that reported favorably to the Board of Executives towards the end of 2000. Other options should also be explored, always in the context of maintaining the MDBs' financial integrity. For example some small portion of the callable capital of EMEs might be tapped to borrow in the markets, financing a special (higher-risk and higher-cost) special window for lending to private sector and other non-sovereign entities.

[34] Guaranties, like loans, should enhance policy reform and encourage countries to move toward international standards.

[35] The World Bank provided a rolling credit guarantee to Argentina in 1998. The Bank guaranteed the first year of an Argentine five-year issue; once the Argentine government made payment on the first year, the World Bank rolled its commitment over to the second year, and so on.

Annex[*]

This annex offers additional background and analysis on a number of issues included in the report. Section I provides background on the set of emerging market economies and their evolving relationship with the MDBs. Section II focuses on the combination of increasing criticisms and demands on the MDBs in the 1990s. Section III looks at the MDBs as agents in the larger global economic system and addresses issues of representation and accountability. Section IV looks at the potential for MDB financing as a catalyst for private investment. Section V explores the issue of financing regional and global public goods. Section VI outlines the World Bank's experience with the provision of fee-based advisory services. Section VII details the evolving relationship of the MDBs in three EMEs; China, Poland and Chile.

I. The Emerging Market Economies (EMEs)

We use an informal definition for a set of "emerging market economies" that includes any country that is in the top 20 of all developing and transitional economies in receipt of net private inflows in the period 1995-98, either in per capita or in absolute terms. Table 3 lists these countries, denoting them by per capita income.[1]

The amount of private capital going to these 'emerging markets' during the 1990s increased dramatically (Table 1). Flows from the private sector to these countries in the 1980s were six times that of the MDBs (MDB flows in a number of countries, e.g. Colombia, Peru, Panama, were nearly equal to private flows). The ratio of private to public flows increased in the 1990s, peaking in 1994 when private flows were over 80 times greater than MDB flows, before private flows fell and the MDBs began emergency lending to mitigate crises (see Table 7 for detailed country breakdowns). In 1998, the private sector was still transferring nearly 20 times more resources, including for direct investment, to these countries than the World Bank and the other MDBs.

In absolute terms, private flows have been heavily concentrated, with 70 % in 1994 going to 10 large countries. However, in per-capita terms, private flows have been high in some small countries too, including in Uruguay, Croatia, and Panama.

MDB lending in the 1990s has been heavily concentrated in this group of emerging market economies, a point that the Meltzer commission highlights (see Table 6 for detailed country breakdowns). Over the past seven years, 80% of World Bank lending has gone to countries with an international bond rating of B or higher. Between 1993-

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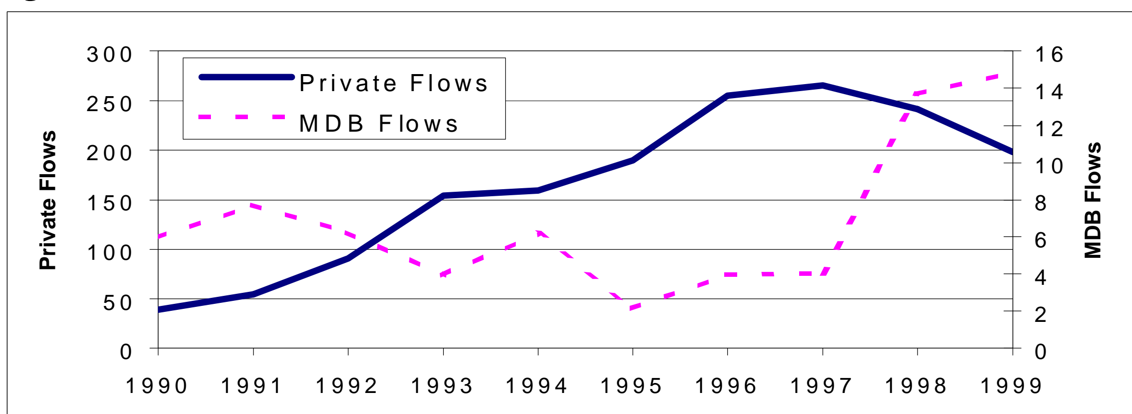
[*] This annex was compiled by staff of the sponsoring institutions and is designed to offer factual background. Its specific contents have not necessarily been endorsed by commission members.

[1] This set includes all of the countries classified as 'middle income' by the Meltzer commission (Uruguay ranks 21st in per capita net inflows of private capital), as well as countries like Russia and China, which can be classified as emerging markets because of their large share in the world's private capital flows. The following countries from this set had an investment grade rating as of March 23, 2001 (Standard and Poor's): Chile, China, Croatia, Czech Rep., Estonia, Hungary, Korea, Malaysia, Poland, South Africa, Thailand, Uruguay.

1999, 11 countries received 70% of IBRD commitments, all of which are in our set of emerging market economies.[2] (These 11 countries are also home to nearly 80% of the population of IBRD countries and about 80% of all the poor in IBRD countries.[3])

Though of a different scale, (Figure 1) net flows from the MDBs in the 1990s have tended to move counter-cyclically to private flows. MDB lending to emerging market economies appears to decline when these countries can more easily and cheaply tap private markets and to rise when, as during the financial crises of the second half of the 1990s, they cannot.

Figure 1: Net Flows to the EMEs in the 1990s ($US Billions)



Source: World Bank, Global Development Finance, 2001 (CD-Rom).

The secular trend of increased access to private markets has affected the scope and size of MDB lending to these countries. For example, in China, the World Bank and ABD have continued to lend in areas where they can provide technical additionality; in Chile, borrowing from the World Bank has ceased, but the Government has purchased advisory services; and in Poland, World Bank lending in the second half of the 1990s has shifted towards support for smaller, more specialized projects and for Poland's bid to join the EU. (See Appendices).

II. The MDBs in the 1990s: new criticisms, new demands

Two big issues in the 1990s were lightning rods for criticism of the MDBs. In the poorest countries, accumulation of unmanageable debt to the World Bank and the regional banks (along with other official creditors) raised serious questions about the effectiveness of multilateral loans.[4] Beginning in the 1980s, and increasing during the financial crises in

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[2] Meltzer (2000). These countries were: China, 12%; Argentina, 10%; Russia, 9%; Mexico, 7%; Indonesia, 7%; Brazil, 7%; Korea, 6%; India, 4%; Thailand, 3%; Turkey, 3%; Philippines, 2%.

[3] Salop (2000). 78% of the poor in IBRD countries (persons living on less than $1 a day) reside in these 11 nations.

[4] None of the countries with unmanageable debt is in our emerging market category. Most have been characterized by low or even negative rates of per capita income growth. Their debt burden has raised the question: Why did official lending continue when apparent returns to the resulting investments were too low for countries to manage servicing those loans? See Birdsall, Diwan, and Claessens, (2001).

Mexico in 1995, East Asia in 1997, Russia in 1998 and Brazil in 1999, the MDBs participated in the financing of huge rescue packages. The IMF took the brunt of the criticism in these cases but the MDBs were also faulted for straying from their fundamental mission and development task, for kowtowing to U.S. or other major shareholders' narrow interests, and for attaching unreasonable conditions to their loans.

Declining trend in lending and increased costs of doing business

Throughout the 1990s, the World Bank and the regional banks were in a constant process of reforming and adjusting to these various critiques (as well as the host of new demands and mandates addressed in the introduction of the report). Even with those adjustments political capital has been lost. There have been real costs (for example, the cost of severance packages for staff declared redundant) and intangible ones, such as slumping morale and reduced ability to attract and retain staff.

Meanwhile, the long-term trend of demand for borrowing from middle-income countries appears to be declining. In the World Bank. loan commitment for 1999 and 2000 were at levels below the early 1980s, and lower as a share of GDP of those countries. World Bank investment lending to middle income countries has been steadily declining since 1994. Investment lending to middle income countries grew rapidly in the 1980s and early 1990s, due primarily to an increase in average project size from $50-80 million in 1980 to $120-160 million in 1994. Since 1994, investment lending has sharply declined to middle income countries (due to a decrease in both the number of projects and the average project size) and the 2000 figure of $6.5 billion in investment lending was the lowest in twenty years.

The decline has been partly muted by temporary increases in "policy-based" lending (to mitigate financial crises), but may foretell a long-term trend of shrinking demand for MDB financing in volume terms.[5] In addition, the demand for smaller, more specialized loans in areas of non-traditional MDB lending seems to be increasing. These types of loans – for technical and institutional services, the provision and monitoring of environmental and other global public goods (GPGs), social sector activity aimed at equitable development etc. – are more costly per dollar loaned for the MDBs to administer and monitor. Likewise, the demand for MDB non-lending services (e.g., advisory services, best practice expertise, country economic and sector work) is increasing as well.

As a result, it has become more expensive to be in the MDB business. There are a number of ways to measure the cost of doing business in the MDBs, all of which are imperfect. One measure is the ratio of administrative costs to the dollar value of annual disbursements. In the case of the World Bank, this ratio has tended to increase in the 1990s, with the exception of the big emergency disbursements in 1997 and 1998. The ratio increased from 5.5 cents in administrative expenses per dollar disbursed in 1980 to a high of 7.8 cents in 1994, and back to 6.9 cents in 2000 after the crisis period (Figure 2).

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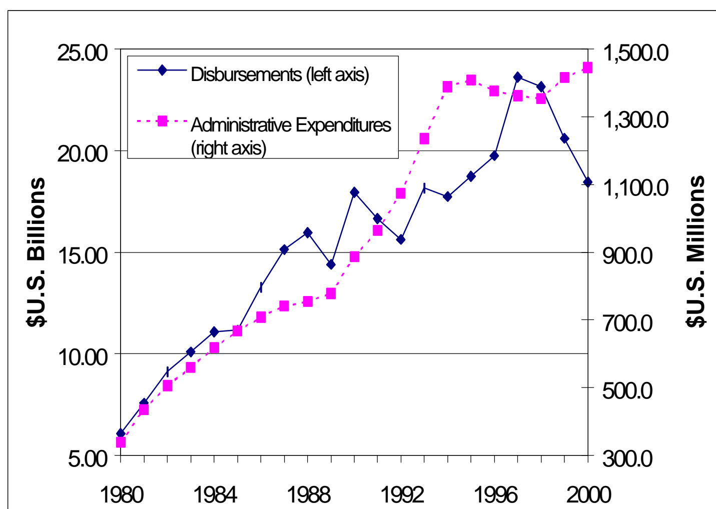
[5] The average World Bank project size to upper-middle income countries was less than $100 million in 2000, down from nearly $130 million in 1991. This is due to a dramatic decrease in the average size of investment loans, while the size of adjustment loans actually grew during this period as a result of large crisis packages.

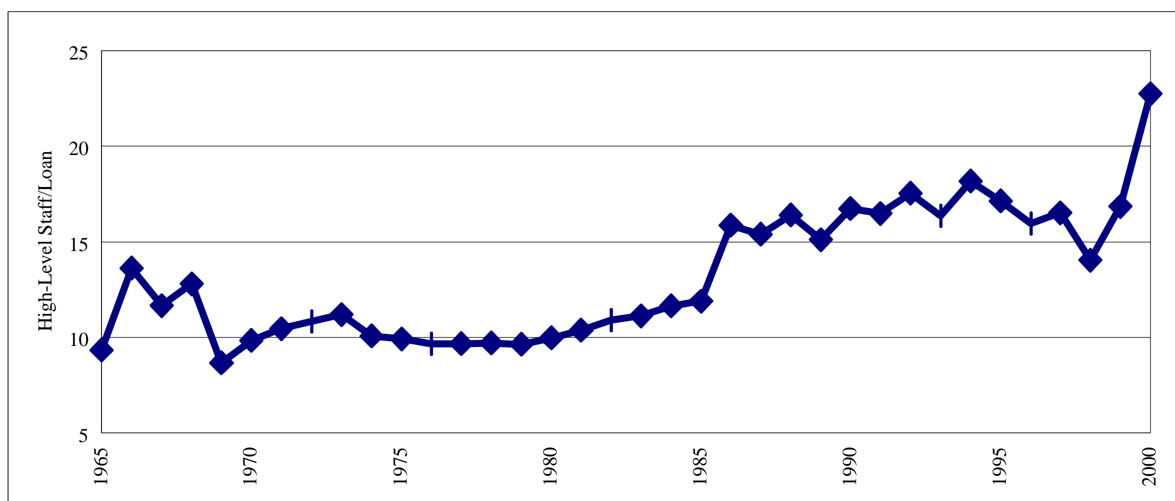
Figure 2: Annual World Bank Disbursements and Administrative Expenses (1980-2000)



Source: World Bank Annual Reports.

Another way of gauging the cost of doing business is the ratio high level staff per loan. This measure captures the costs, in staff time, of executing individual MDB loans. Figure 2 shows this relationship for the World Bank since 1965. After fluctuating in the late 1960s, the number of staff per loan remained steady through the 1970s, and began increasing in the early 1980s. The number continued to rise in the 1990s, and despite a dip in 1998 (due to the large outlays from emergency loans) reached its highest level ever in 2000 (due primarily to a decline in the number of loan operations).

Figure 3: High-level Staff per Loan/Credit (IBRD/IDA)



Sources: Data until 1990 for both loans and "professional staff" comes from World Bank Annual Reports. After 1990, loan data comes from Annual Reports and "high-level staff" data, comparable to "professional staff" measure, was compiled from an internal compendium of personnel statistics.

At the moment, the MDBs are generating sufficient net income to sustain operations without having to alter their underlying capital structures.[6] Assuming no change in financial policies, lower levels of lending ultimately imply either higher costs for the banks' borrowers, or reduced administrative spending.

III. Representation and accountability: the MDBs in the global economic system

The MDBs are only a piece of a larger system that changed and adapted slowly to the increasingly globalized environment.[7] In the 1990s there was some progress in strengthening what might be called the global system of economic governance. This was true on the finance side particularly following the Asian financial crisis (e.g. the creation of the Financial Stability Forum), and in development (the donors in 1999 agreed on a common set of 'international development goals' for poverty reduction).[8] But given the increasing stake of the emerging market economies in the global economy, and their potential to affect its growth and stability, they are not well represented in decision-making fora at the global level. Recognition of the problem in the past few years led to increasing efforts to include EMEs in discussion of the international financial architecture, through creation of the "G-20" (G-7 plus Argentina, Australia, Brazil, China, India, Indonesia, Mexico, Russia, Saudi Arabia, South Africa, South Korea, and Turkey). (Also head of WTO; UN Security Council).

Projections of the future role of the EMEs in the global economy reinforce this point. The OECD estimates that "the big five" (Brazil, Mexico, China, India and Russia) will substantially increase their shares of world GDP and world trade by 2020. When global population levels off at roughly 9 to 10 billion people in 2050, India and China with Africa will constitute the global majority.

The governance of the MDBs has been relatively effective in terms of its purposes and foundations, compared to the one-country one-vote system in the UN system. Decision-

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[6] An internal World Bank Task Force on Middle Income Countries has defined an informal 'zone' for its annual lending commitments above which would translate into larger net disbursements and more risk for its existing capital and below which would not generate adequate net income to cover its administrative costs, its current ability to waive certain charges on borrowers, and its shareholders (mostly non-borrowers) desire to use net income to finance transfers to IDA, HIPC costs, and various other grant-making activities of the Bank. During 1998-1999, the World Bank neared the upper level of this zone (estimated at $18-21 billion) and the following year came close to its lower limit ($9-12 billion). If the trend of decreased lending continues this could potentially be a more serious problem.

[7] The World Bank and the other regional and sub-regional development banks have constituted one of three main parts of the global economic system in the postwar period. The International Monetary Fund, the twin institution founded with the World Bank in 1945, has been principally concerned with maintaining financial stability (though increasingly involved in developing countries over the years, where the distinction between the policy and financial demands of domestic stability and growth is difficult to define); and in 1995 the World Trade Organization succeeded the General Agreement on Trade and Tariffs as the global institution supporting trade. The World Bank and the four large regional banks also constitute a central part of the global development system. MDB loans for development purposes are one part of a larger flow of so-called "overseas development assistance" (ODA) to middle-income as well as poor countries. Other ODA includes primarily loans and grants of governments in Europe and Japan, and technical assistance of the various agencies of the United Nations.

[8] See "A Better World For All," (2000).

making is in broad terms aligned with financial responsibility and burden.[9] Yet in the World Bank in particular, there is a growing distinction between the relatively low costs associated with capital ownership by the US and other non-borrowers and their power in the decision-making process.[10]

Large borrowing members' relative lack of influence has created tension about financial decisions that are seen as priorities of non-borrowers, such as the use of net income for the HIPC initiative or for the financing of global public goods initiatives such as the Global Environmental Facility. More generally, there is a difference in emphasis between non-borrowers, who emphasize the banks' role in poverty reduction and other priorities such as environment and governance, vs. borrowers, who seek the banks' lending and advice in order to accelerate growth. To the extent that ownership of economic reforms supported by MDB lending affects implementation of reform in EMEs, lack of influence of borrowers in general may undermine the effectiveness of the banks in their lending programs.[11] This is less likely to be a problem in the IDB and ADB, compared to the World Bank, because borrowers as a group control about 50% of the votes (on most decisions), and in the IDB the President is by design from a borrowing country.

IV. MDB Financing as a Catalyst for Private Capital

The strategic aim of much MDB lending is to strengthen the institutional capacity and policymaking tools in developing countries to create an environment that is conducive to increased private investment. Many emerging market economies still cannot issue debt at manageable costs or for terms beyond five to seven years, yet development investments—in schools, roads, and municipal reform—have much longer gestation periods. Many of these investments have limited financial returns (though high economic returns), and will not be directly financed by the private sector without a government guarantee. The private sector is, of course, indifferent to a sovereign government's use of borrowed funds. But where sovereign borrowing is not possible at reasonable cost, governments without MDB financing would have to finance schooling and roads with medium-term money, with a resulting costly and risky mismatch of asset and liability tenors. MDB loans help ensure that these investments are financed, and, when these investments are successful, they create a climate for increased private investment in more commercially attractive sectors.[12]

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[9] In the World Bank, decision-making power is concentrated with the high-income nonborrowing member countries (non-borrowers control 62 %). In the regional banks borrowers have a higher proportion of shares (about 50%), although the banks borrow only against the capital of the nonborrowers and thus the banks' operations are still fundamentally completely dependent on the nonborrowers financially.

[10] The political visibility costs of membership for non-borrowers – in terms of the need for legislatures to appropriate budget funds – have virtually disappeared. Many believe in particular that the U.S. has exercised influence in the MDBs (and the IMF) far exceeding its share in the financial burden.

[11] The problem of representation and governance of the banks may also explain difficulties in a number of areas. Among them are problems in increasing the transparency of policy-based operations (the documents of which are, in the World Bank, still not disclosed to the public after approval), and tension over the nature and extent of conditionality (e.g. during the Asian financial crisis whether policy conditionality reflected lack of any accountability to citizens and workers in Korea vs. creditors in the U.S. and Europe).

[12] [Birdsall, Diwan, Brady deal analysis] Dollar and Pritchett (1998), Collier and Dollar (1999), World Bank Task Force Report Annex (Forthcoming). Qualitative assessments (interviews conducted by Sussex 200)

With privatization of formerly state-owned enterprises, most governments of the EMEs now rely on private lenders and investors to finance new investments in power, telecommunications, transportation and increasingly in water and sanitation and waste management and other environmental services. MDB lending in these sectors has shifted accordingly from directly building and operating projects to support for enhancing the regulatory structure – in an attempt to attract greater flows of private capital and maintain a catalytic role.

MDB financing in emerging markets may also encourage private investment by providing information and a seal of approval for a country's institutional capacity. This is most likely to be important in particular sectors (such as water, where the private sector sees MDB sectoral support as a signal) and in the smaller emerging markets where the costs to private lenders and investors of acquiring and assessing information are high. In these countries, MDB involvement in a particular sector can implicitly endorse a country's institutional capacity and the overall status of its economic management. Middle-income country officials tend to cite this kind of benefit as one reason for continued demand for MDB assistance.[13] Rating agencies (most notably Moody's and Standard and Poor's) provide a similar service, though usually not at the sectoral level. And even at the country level, they may carry less weight with private investors than do the MDBs, whose lending activities mean they have good information and whose balance sheets are at stake.

V. Financing Regional and Global Public Goods (GPGs)

The MDBs, and particularly the World Bank, have been under ever-increasing pressure to finance and provide a variety of non-lending services that constitute regional (trans-border) and global public goods.[14] Examples at the World Bank include management and partial financing of the CGIAR (network of agricultural research institutes) since 1971; shared management of the Global Environmental Facility; creation and initial financing of the Global Development Network (of policy research institutes around the world); creation and financing of InfoDev to attack the digital divide. The IDB has sponsored such regional programs as the technical secretariat for the Free Trade Area of the Americas negotiations; a regional agricultural research consortium (Fonagro); and grants for development of a sub-regional electricity grid (Central America) and for environmental assessment of other potential trans-border infrastructure projects (Hidrovia, Parana River). In addition, of course, the research, analytical work, and shared experience on best practice (in agriculture, health, education, finance, etc.) financed in the core administrative budgets of the banks as the basis for country lending constitute public goods.

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suggest that MDB involvement can facilitate an environment where the private sector operates more effectively.

[13] As reported in World Bank, 2001 (draft).

[14] GPGs are characterized by non-rivalrous consumption (the consumption of one individual does not detract from that of another) and non-excludability (an individual can not be excluded from enjoying the good). Regional public goods, or local public goods, are those that fit the definition of a GPG but are limited geographically.

Extra-budgetary GPG activities are financed in grant form by special donations of donor governments to trust funds managed by the MDBs, or directly by MDB income, including income from lending. Income of the World Bank has been periodically transferred to supplement that bank's concessional window. In the World Bank, the IDB and the ADB, income is being transferred to finance a portion of those banks' share of debt reduction for the poorest countries (HIPC) – considered a global good (aid and debt reduction for the poorest countries of the world).

The growing interest in RPGs is evident in the proliferation of regional and sub-regional trade agreements in the 1990s. The regional development banks (RDBs) are also well situated to facilitate regional infrastructure projects and harmonize regulatory systems relevant to finance, transport, food safety and so on.

The provision of regional and global public goods by the MDBs is thus not new. Nor is it surprising; these are existing institutions with the expertise and infrastructure to undertake "global" tasks. The tasks need to be financed separately from the traditional loan windows of the banks because the allocation of benefits, and thus the cost of borrowing is not clear. (No single government is willing to pay borrowing costs for benefits it cannot fully capture.)

The challenge for shareholders is to make transparent and systematic the sharing of the costs of GPGs and RPGs among themselves. From the point of view of the largest borrowers and indeed all the EMEs, use of income from lending operations to finance global goods imposes a cost on them (since it works its way back to higher loan charges to reach income targets). From the point of view of the non-borrowers, because the loans are subsidized by their guarantee of the MDBs' liabilities, the effect on the cost of borrowing is not a measure of the cost of financing regional or global public goods.

VI. World Bank Fee-based Advisory Services

The World Bank has charged for the provision of advisory services, but until this point it has been done on an informal, ad-hoc, basis. The most prominent example of this activity is with Chile (see Section VII), and another is with the oil producing nations of the Middle East and North Africa.

Beginning in 1975, the oil-producing nations, suddenly awash in funds as a result of skyrocketing oil prices, began to seek advisory services from the World Bank to ensure that these funds were spent wisely. The Bank provided these services on an informal, ad-hoc basis, charging the clients slightly below cost. During the late 1970s, Saudi Arabia paid the Bank approximately $5 million per year for advisory services rendered. That figure has since fallen to about $2-3 million per year. Kuwait, Oman and the United Arab Emirates also pay fees of approximately $200-300 thousand per year to the Bank for advisory services.

The Bank's advisory services to these countries have been focused on infrastructure, macroeconomic policy and education. Some of the particular advisory services include: (1) an education sector assessment for Saudi Arabia; (2) evaluation of industrial complexes for Saudi Arabia; (3) supervision of the construction of the Causeway civil works project connecting Saudi Arabia and Bahrain; (4) an economic and sector work (ESW) entitled, *Vision for the Future,* for Kuwait; and (5) advice on the construction of a university in Saudi Arabia.

VII. The evolving relationship of the MDBs in EMEs: China, Poland and Chile

China

In 1980, China was one of the poorest countries in the world; 80 percent of the population lived on less than $1 a day, and two-thirds of the population was illiterate. Three decades of Maoist rule had left China's economic institutions and physical infrastructure in disarray. The focus on state led production in an economy based primarily on traditional agricultural production (31.2% of GDP) provided little foundation on which to build a market economy (private sector activity accounted for just 0.9% of GDP in 1980). The new Chinese leadership under the direction of Deng Xiaoping recognized that to embark on an economic liberalization program and revive its economy, China would need extensive technical and financial assistance. China became an official member of the World Bank in 1980, and of the ADB in 1986 with the hope that these multilateral institutions would offer some of the capital, expertise, and credibility necessary for this restructuring.

After surveying the state of the economy, the Chinese government, in collaboration with the World Bank, identified six crucial areas in which China needed the financial and technical assistance. These areas were: macroeconomic policymaking, social sectors (particularly education), project management, environment, physical infrastructure, and poverty alleviation (particularly rural poverty). The World Bank and the ADB have concentrated their activities in these areas of expressed need.

Since 1980, the World Bank's support in each of these areas has been rooted in analytic studies called Economic and Sector Work (ESW). Three multi-volume ESW reports have underpinned the Bank's macroeconomic policy advice in China. In 1981, the Bank produced the first comprehensive description of the Chinese economy, including the first estimates of China's GDP. In 1987, the Bank published a forward-looking analysis of the economy, along with projections for performance in the 1990s. Most recently, in 1995, the Bank published the "2020" report, analyzing the factors likely to influence China's economic performance from 1995 to 2020.

Macroeconomic policymaking. In 1980, the Chinese government had essentially no experience in formulating macroeconomic policy. Bank staff studied the sectoral composition of the economy and assembled the nation's first modern national income accounts. The Bank provided the capital and knowledge required to implement measures

for the collection and processing of data and familiarized the Chinese with the guidelines of managing a market economy.

Social sectors. With rampant poverty and a sprawling population, China faced severe troubles in its social sectors, particularly university education. With the assistance of the Bank, the Chinese crafted a new, comprehensive education strategy, which put emphasis on teacher training, writing and production of textbooks and vocational training. The first operation financed by the World Bank involved upgrading university education by modernizing curriculum and introducing new subjects.

Project management. Both the World Bank and the Asian Development Bank also provided China with expertise in project management. Both banks brought skilled engineers, economists, financial experts, sectoral specialists and managers to help ensure the technical soundness of projects while cultivating local expertise in these areas. (Chinese officials repeatedly indicated to the World Bank management that one of the most important contributions made by the Bank was the introduction of international competitive bidding (ICB), which saved the country a significant amount of public resources. The Chinese went on to introduce ICB in government procurement of projects financed from domestic resources.)

Environment. China's state-led drive toward rapid industrialization came at the expense of considerable damage to its ecological environment. China's environmental problems were compounded by its large population and its reliance on coal as a source of energy. The World Bank has supported Chinese efforts to minimize adverse environmental impacts. Specifically, the Bank brought clean coal technology to China and re-established district heating in some of the larger cities of the country, significantly reducing the level of sulfur and other pollutants in the air. The Bank also funded a $300 million reforestation project and cleanup of polluted rivers in Shanghai.

Physical infrastructure. Physical infrastructure was, and continues to be, one of the most daunting constraints to economic growth in China due to the country's enormous population and rapid pace of expansion. Domestic, bilateral and private sources were never able to provide the amount of capital required for infrastructure investment. Both the World Bank and the ADB have supported investments in modernizing and expanding China's ports, roads, bridges, power production and distribution and telecommunications infrastructure to prevent bottlenecks. The ADB has concentrated about two-thirds of its lending to China in the energy/power and transport sectors, and the World Bank about 60% (cumulative lending stands at $35 billion) to infrastructure.

Poverty alleviation. From 1991-2000, the World Bank lent over $3 billion on projects targeted to the poor for investments in agriculture, rural health, education, rural roads and rural water supply. The Bank committed considerable resources to improving the efficiency of agriculture and agribusiness primarily through IDA. Since 1981, the World Bank loaned $9.6 billion to promote market-based, sustainable development of agriculture and agribusiness. China has also drawn on the World Bank's capital and civil engineering

expertise to implement numerous voluntary resettlement projects, without which the country could not have implemented large infrastructure projects.

Twenty years after becoming a member of the World Bank, China is among the fastest growing economies in the world, with an average annual growth rate of over 10% since 1980. The economy has been greatly modernized. Services now account for 32.9% of output and exports now represent 22.1% of GDP. FDI flows into the country at a rate of about $40 billion per year. Since 1978, China has also established a strong record of poverty alleviation, reducing by 220 million the number of people living in absolute poverty. Life expectancy has risen to 70 years and 83% of the population is now literate.

In July 1999, China officially ceased borrowing from IDA, the highly concessional window of the World Bank. China in recent years has attracted around $40 billion per year in FDI. Among challenges for which China is likely to continue to pursue financial and technical support are: managing China's entry into the WTO; designing new analytic work; meeting the near $1 trillion need for additional investment in infrastructure; modernizing the financial sector and pension systems; and transferring resources to the interior provinces for poverty reduction.

Poland

Poland is an example of one of the most successful transitions from a planned to market economy. On the heels of a historic transfer of power in 1990, the newly assembled 'solidarity' government, led by Tadeusz Mazowiecki, initiated a comprehensive set of 'shock therapy' reforms that transformed the Polish economy. In 1994, Poland was the first transition economy to get back to 1989 GDP levels, and by 1995 was receiving high levels of private capital and foreign direct investment (FDI). Aided by a strong macroeconomic policy strategy, and a quick and successful privatization program, Poland has sustained high levels of growth and development throughout the 1990s. Despite the Russian financial crisis, Poland managed 4% growth in 1999, due primarily to strong domestic demand.

Throughout this period of transition in the 1990s, a number of multilateral development institutions have played an important role in Poland's economic growth. The evolving relationships between Poland and three of these multilateral institutions – the World Bank/IFC, EBRD, and EIB – are detailed below.

Trends in World Bank lending

Poland was one of the founding members of the World Bank in 1945, but withdrew with the Soviet Union in 1948. Poland rejoined the World Bank in 1986 and was issued its first new loan in 1990. After committing significant resources to aid the transition in 1991, the World Bank has played a continually decreasing role in Poland throughout the 1990s, as the availability of private capital and FDI have increased (Table). This decrease in financing is in contrast to sharp increases in financing from other multilateral institutions

(explained below). World Bank flows also display a generally counter-cyclical tendency, increasing in 1994 and again in 1999 in response to decreased levels of private capital, and decreasing in the 1995-1998 period when the level of FDI and private capital nearly doubled in Poland (the jump in IBRD commitments in 1998 can be partially explained by a $200 million emergency flood relief loan).

Table: Poland in the 1990s – World Bank activity and Private Capital Flows

	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	Total
IBRD Net financial flows, (current US$ millions)			54.1	349.3	342.8	317.0	672.3	191.3	266.3	83.6	-22.6	…	…	
IBRD lending commitments (millions of US$)			781	1440	390	900	146	215	181	67	522	327	161	5130
Private capital flows, net total (current US$, DRS)			71.1	535	723	2158	1244	5058	5333	7302	9653	…	…	
Foreign direct investment, net inflows (% of GDP)			0.1	0.4	0.8	1.9	1.9	2.9	3.1	3.4	4.0			
GNP per capita (constant 1995 US$)	2992	3002	2871	2703	2780	2895	2998	3221	3442	3672	3833			
GNP per capita growth (annual %)	3.89	0.34	-4.37	-5.85	2.85	4.12	3.56	7.42	6.87	6.69	4.38			

Data Sources: World Bank; World Bank World Development Indicators CD-Rom; World Bank Global Development Finance CD-Rom.

An evolving relationship

IBRD activity in Poland can be separated into two periods. Between 1990 and 1995, the World Bank committed significant resources to large projects, including for infrastructure, to help with the massive task of economic restructuring (average project commitment size during this period was $183 million). The IBRD's first approved loan to Poland is indicative of this period; in February 1990, a commitment of $260 million to increase the volume, quality and value-added of industrial exports to convertible currency markets. In 1991, the IBRD followed with its largest commitment of $340 million to restructure Poland's energy and electric power sector, and committed an additional $240 million to help Poland design and implement its privatization program. Between 1990-1995, the IBRD made significant lending commitments ($100 million +) for infrastructure development in all of the following areas: energy resources (oil and gas), telecommunications, financial institutions, health, housing, and roads.

By 1995, Poland achieved an impressive level of economic stability, and, was given an investment grade rating for the first time since the transition. Poland also concluded London Club negotiations to forgive 50% of debt in 1994, which complemented a similar Paris Club negotiation in 1991. These and other factors helped Poland make a successful return to the international credit markets.

In response to both Poland's increased standing in private capital markets, and the possibility for EU membership, the World Bank began to shift its activities in Poland from investments in structural and macroeconomic reforms, to increased lending for social sector development and advisory services. The World Bank scaled back its overall lending commitments during this second period (1995-2000) and focussed on smaller social sector

and environmental loans (average project commitment size during this period was $95 million). In 1999, the World Bank initiated its first Adaptable Program Loan (APL) in Poland – designed to offer a more flexible and non-traditional approach to the design and implementation of long-term projects. (The APL in Poland supports a Rural Development Project aimed at facilitating private sector investment in less developed rural areas to create new off-farm employment opportunities.)

This change in the scope and size of lending was a response both to Poland's emergence as a hot spot for inflows of private capital and also to its new status with the EU. After the European Commission's decision to begin the EU enlargement process in 1997, the World Bank focused its efforts on helping Poland reach the EU environmental and social targets. While Poland's strong macroeconomic policies effectively tamed inflation and stimulated growth, there are still a number of social problems – most notably unemployment (13% in 2000) and management of environmental issues – that need to be addressed. In 1997, the World Bank prepared a detailed advisory document titled "Reform and Growth on the Road to the EU" that laid our challenges and strategies for Polish EU ascension. In 2000, all three of the World Bank's approved loans to Poland (totaling $160 US million) focused on environmental and social development issues in line with this strategy.

The World Bank's IFC has also been active in Poland in the 1990s, and its lending activity exhibits a similar trend. The first IFC local office was opened in Poland in 1990, and since that time, the IFC has approved over $US 550 million for projects with a total cost of over US $ 2 billion. In the beginning years, the IFC was heavily involved in privatization and SME development, usually in partnership with European and other international banks.

After 1995 when Poland began receiving large inflows of private capital, those types of services were less in demand. Poland no longer needed the IFC as a liaison to crowd-in additional investment. Accordingly, the IFC has turned its attention to non banking financial institutions, focusing in areas of leasing, insurance and private pension fund management. The IFC is also beginning to explore social sector financing for specific private sector projects in education and health. The World Bank has traditionally had a mandate to provide funding for these areas, so the IFC has been slow and cautious to develop its social sector lending facilities.

The IFC has also offered a range of non-lending services. One example of this is the Polish Business Advisory Service (PBAS). Designed to provide advisory services as part of the post-privatization strategy of the World Bank Group, the PBAS completed more than 150 advisory assignments, generating $24.9 million in project financing between 1991-1996.

The EBRD and Private Sector Development

Poland has been one of the EBRD's largest borrowers since 1991, signing 102 investment projects involving an investment of over 1.3 billion Euros (Table). The total

amount of EBRD financing underestimates the impact of EBRD activities, as many of EBRD undertakings are joint partnerships (where the bank is providing a small portion of the financing as well as a guarantee). It is estimated that EBRD investments have mobilized an additional 575.1 million Euros in investment during the 1990s. Almost 90% of EBRD financing has been provided for private sector projects. About one quarter of the EBRD's finances have been in equity investments, and about three-quarters in debt. Unlike World Bank commitments, EBRD financing has been somewhat pro-cyclical, and has increased in the second half of the 1990s to support the rapid inflows of private capital in Poland. The EBRD's lending focus has been on the private banking sector and on non-traditional, non-infrastructure sectors like communications, agribusiness and equity funds.

Table: The EBRD in Poland

Financing per Year (in Millions of Euros)			**Financing by Sector**			
1991-92	88.5		Bank	13.7%	Steel	5.0%
1993	111.3		Communications	10.1%	Cement	3.8%
1994	165.7		Agribusiness	9.9%	Energy	3.7%
1995	69.8		Equity Funds	9.0%	Railways	3.5%
1996	228.4		Auto	5.7%	Paper Products	3.4%
1997	191.7					
1998	343.2		**Composition**			
1999	156.3		89% private, 11% public			
Total	1354.5					

Source: Data compiled from EBRD.

From the beginning, the EBRD has tried to adopt a strategy that is in line with, and provides additionality to Poland's strategy for economic development and growth. Because of this, EBRD strategy has changed with the pace and direction of the Polish transition. Since 1995, the EBRD has placed increased emphasis on assisting the rapidly changing private investment environment, and has begun to switch its finances from debt to equity, and to move outward from the city of Warsaw to support the outlying provinces. While the EBRD has continued to assist the government in the privatization process, it has placed increased emphasis on involving more small-to-medium sized enterprises (SMEs) through a combination of debt and equity. The bank is currently implementing the EC-EBRD SME facility and providing dedicated credit loans to local banks.

The EIB

Poland has received significant additional resources from the European Investment Bank (EIB), the European Union's financing institution. Since 1990, the EIB's EUR 3.8 billion in project lending to Poland is more than to any other EU candidate (26% of all EIB lending in the 10 CEE EU candidate countries has gone to Poland). More than EUR 2 Billion of the EIB's lending has come since 1998. This financing has come during a period of increased private capital flows and decreased World Bank lending.

About EUR 1 billion of EIB activity in Poland has financed Poland's part of the 8-country Trans-European road and rail Networks (TENs). The EIB has also financed telecommunications, gas and industry projects, and has set up a program to help support SMEs in the region. The EIB also provided emergency funds to help with reconstruction of infrastructure after the 1997 flood.

Chile

In the past 15 years, Chile has become one of Latin America's great success stories, undergoing profound economic, social, and political change. The important structural reforms the country maintained and deepened after the 1982-83 crises led to increased domestic savings, lower inflation rates, and increased investments—paving the way for remarkable economic growth rates.[15] By the early 1990s, high domestic savings rate and continued balance of payments surpluses, coupled with ready access to international financial markets, redefined Chile's relationship with the multilateral development banks. In 1994, the country started to use its own funds to finance the bulk of its public investment programs. A year later, it prepaid $540 million of outstanding debt to the World Bank and $727 million to the Inter-American Development Bank. Private capital flows to Chile also increased significantly.[16]

For the remainder of the decade, the Banks would move away from large loans to a focus on technical cooperation, advisory services and limited financial assistance in areas such as rural development, technology and the environment.

Chile and the World Bank

In 1995, following more than a decade of intense support for economic reforms and other programs, the World Bank's program of activities for Chile started to decline. The Bank had been a major supporter of reforms undertaken in the latter part of the 1980s, lending close to $ 1.3 billion from 1985 to 1990, of which $ 750 million was quick disbursing, policy based lending. But by the time the Bank's country strategy was drafted in 1995, it had become clear that there was far less rationale for lending, and, although not excluded per se, new lending would be more selective and at a lower level than in the past.

Nevertheless, the Chilean government remained interest in maintaining its relationship with the Bank to benefit from the Bank's analytical capacity. Ongoing loans provided the opportunity for the normal exchange of technical and policy advice to continue (by 1995, there were still 13 projects under implementation, with about $ 535 million undisbursed). In addition, the Chilean government began paying the Bank for advisory work on topics responsive to the country's economic and social priority.

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[15] The important structural reforms included trade liberalization, capital and labor market reforms, privatization, the creation of a regulatory framework, and social and pension reforms. In the 1990s, Chile enjoyed one of the world's highest growth averages, 6.5%.

[16] In 1995, the flow of private capital to the country (US$ 5.5 billion) was four times what it had been just four years earlier.

Lending

From 1995 to 1997, Chile did not borrow from the IBRD. In the following two years, the country also selectively reduced undisbursed loan balances by canceling amounts which it did not anticipate using. In 1998, several new projects were approved, concentrated in education, technology, public sector efficiency, and the environment. In addition, Chile became active in the Bank's GEF mid-size grant program introduced in 1998 to provide grants to non-governmental organizations.

Evolution of Chile's External Debt and Resource Flow (US$ million)				
	1979	1989	1998	1999
Total debt outstanding and disbursed	9,361	18,032	31,691	37,007
IBRD	158	1,618	945	912
IDA	21	15	9	8
Total debt service	2,089	2,668	4,481	3,930
World Bank Program				
Commitments	0	574	0	5
Disbursements	13	205	71	43
Principal repayments	7	108	106	111
Net flows	6	96	-35	-68
Interest payments	15	116	59	71
Net transfers	-9	-20	-94	-139

As of 2001, the Bank's portfolio stands at four projects under active implementation and one at the point of closing (as compared to 13 projects in 1995). IBRD support has fallen most sharply for infrastructure, and the Bank has not provided any guarantees for private sector infrastructure as had originally been envisaged in 1995. In contrast to its lending during the 1980s, the IBRD's program during the 1990s did not contain any quick disbursing lending for economic reforms.

The new Government of President Ricardo Lagos (as of March 2000) has indicated that it may wish to continue to borrow selectively. New operations presently being considered include: public financial management, life-long-learning initiatives, and natural resource management.

Advisory Services

In 1996, the Chilean government and the World Bank entered into a formal agreement of reimbursable advisory services. At the time, there was no overall institutional policy at the Bank regarding provision of advisory services. The agreement with Chile was especially designed and it included procedures for how to respond to the government's

requests, duration of assignment, billings, and other details.[17] Specifically, the agreement made provision for: (a) one major study (Economic and Sector Work (ESW)) done at the administrative expense of the Bank per year with a value of the equivalent of about one staff year; (b) ad hoc studies and short -term advice by Bank staff and/or Bank-financed consultants at the request of the Chilean Government.

The assignments undertaken during 1996-98 were as follows:

Private Sector Development and Regulation	**Social Policy and Programs**	**Environment**
• Privatization of airport passenger and cargo concessions-- $ 30,900	• Diagnostic of higher education-- $ 49,100. (This work led to a new loan request to finance improvements recommended by in the study.)	• Development of a new institutional framework for environmental and natural resource management regulations-- $21,800
• Review of toll road concessions and ways to relieve constrictions-- $36,300		
• Modernization of public service regulatory institutions--$ 16,500		
• Inputs to new law of hydrocarbon policy and deregulation--$ 17,300		

In 1996, as the government developed a comprehensive education reform program, it asked the Bank to provide long-term advice. A full time Bank educational specialist was seconded to the Ministry of Education for 18 months. The Bank paid the staff's salary and benefits while the Government paid $ 2,500 per month to cover living costs and other expenses. After the staff member returned to Washington, the Government continued to pay $ 2,500 per month for seven months as a way of ensuring access to continued technical advice.

Regarding ESW, the Bank completed two studies from 1996 to1998: one Poverty Assessment, the Bank's first in Chile (1997), and a Study of Chilean Savings and Tax Policy (1998).

Recent Fee-Based Assignments

In May 1998, following the introduction by the World Bank of a new policy covering fee-based technical assistance, the agreement with Chile was evaluated. By that time, the government had reimbursed the Bank about US$170,000. Overall, the experience was

[17] The advisory services program was intended for assignments of short duration, normally two weeks. The costs of these services included staff time (salary and benefits) plus the direct costs of any consultants and travel. The agreement was to last until the Bank instituted a specific policy on such advisory services and/or up to $200,000 was spent, when it would be subject to review.

considered positive by both parties and a number of recommendations were made on when and how such programs could work in other countries. Since then, Chile's program has been less active. In the last two years, it included a study on Health Insurance Issues: Old Age and Catastrophic Health, in support of a governmental commission on health (1999), a series of Policy Notes (2000), and an update of the Poverty Assessment (2000).

Private Sector: The IFC and MIGA

Financing from the IFC has followed a similar trend to IBRD lending. As the availability of both domestic and foreign long-term financing improved dramatically in the 1990s, the IFC started to limit its financial assistance to projects in nontraditional industries, cross-border operations, large infrastructure projects (requiring longer terms than those usually available), and projects with complex risk-mitigation provisions that justify IFC's involvement.

MIGA's operations in Chile during the 1990s have included guarantees for copper mining facilities such as Minera Candelaria and an Argentina-Chile gas pipelines, which enabled MIGA to provide multi-country coverage i.e., coverage against actions taken by either government that would affect the project enterprise in either country. Chilean investors also looked for MIGA to seek insurance for their investments in other Latin American countries.

Chile and the Inter-American Development Bank (IDB)

Chile's relationship with the IDB evolved significantly in the past decade. Since its creation in the 1960s, the Bank has always been a key partner in Chile's development efforts.[18] From 1974-1989 for example, it was the leading contributor to domestic investments in Chile among multilateral financial institution—helping the country gradually overcome the severe crises of the early 1980s. By the 1990s, however, as Chile started to use its own funds for public investment programs, the Bank's operational flow to the country was drastically reduced. The prepayments of loans and cancellation of pending disbursements covered most operations in the Bank's loan portfolio.

Lending

For the latter half of the 1990s, greater attention was given to the contributions the IDB could offer through technical assistance—especially in the development and modernization of the private sector and civil society. During this time, a number of small national and regional technical cooperation programs were financed. Successful ongoing projects in urban development and planning and reform were continued though the approval of new loans. Private sector participation was actively stimulated, particularly the government's strategy of awarding concessions to open public infrastructure to private sector initiative.

[18] For the past forty years, the Bank has approved 104 loans to Chile, totaling almost US$ 4 billion. Of these, Chile has repaid close to US$ 3.5 billion.

Net Financial Flows, IDB (current US$ millions)									
	1990	1991	1992	1993	1994	1995	1996	1997	1998
Concessional	-1.31	-1.32	-1.33	-1.33	-1.22	-1.35	-1.33	-1.04	-1.04
Nonconcessional	189.2	78.8	100.7	-39.3	-25	-1115	-403	-342.9	-42.8

In 2000, the new government made clear its intention to give new impetus to Chile's operational relationship with the IDB. For 2000-2006, a basic loan scenario was established totaling US$ 600 million—to be concentrated in the first two years and updated regularly. The main challenge for the Bank has been to strike a new balance in the composition of its products. To support the public and private sectors as well as civil society, the Bank must assign equal importance to the development of financial and non-financial instruments.[19] Priority is now focused in 4 areas: help increase competitiveness, reduce social and regional inequalities, and enhance citizen participation and modernization of the state. With better-targeted actions, the IDB hopes to ensure continuity in areas where the government and the Bank have been working together (e.g., decentralization) and to cooperate in new areas in which the Bank has comparative advantage (e.g., support for citizen participation, modernization of government management, and reducing social exclusion).

Non Financial Services

The Banks' new strategy for Chile provides for continuing support for the government's efforts to promote dialogue on issues of economic and social development. In the past year, the IDB designed and co-financed 5 workshops with Chile and promoted a meeting to present its strategy for private sector development. With regards to technical assistance, the intention is to establish a flexible mechanism to provide the Chilean government with advisory services to support specific, short-term undertakings in public policy areas. For this purpose, an Advisory Services Program is now under preparation. It will represent a new technical assistance facility offered by the Bank whereby the government can draw upon short-term advisory services (not exceeding 10 days) to be provided by the Bank's professional staff or by contracted outside consultants.

Private Sector: The Inter-American Investment Corporation (IIC) and the Multilateral Investment Fund (MIF)

The coordination of instruments for private sector development will continue to play a key role in the Bank's strategy for Chile. In the case of the IIC, between 1989-1999, 10 projects were approved in Chile, with funding commitments of nearly US$ 48 million (covering 20% of the total costs of the projects).[20] The majority of these projects have been

[19] In designing this new strategy, the IDB has engaged various sectors of Chilean society (e.g., government agencies, civil groups, private sector, etc.) in continuos consultation process carried through a series of dialogue workshops. The results have helped define specific activities for financing by the Bank's operation programs –especially in tune with the country's main development challenges.

[20] By 2000, 7 out of 10 projects had been executed, representing US$ 37,960 million of IIC funding. Of these, US$ 16.5 million have been repaid, and sales and write-offs amounted to US$ 4.1 million.

targeted to agribusiness and small and medium size enterprises. In particular, the IFC has focused in the export promotion of non-traditional goods helping finance in the mid 1990s expanded productive capacity and technological improvements for small companies seeking to export this type of goods. Future projects will deal with the promotion of exports in areas where Chile has comparative advantages like forestry, fisheries, and mining; the development of basic infrastructure projects such as hydroelectric plants and rails transport; and the creation of new instruments to encourage development of capital markets. Three projects are already under way in forestry development and agriculture and aquaculture processing. Among the programs under consideration for the coming year is an operation with a local financial institution to create an investment fund and a debt facility in support for SMEs.

The MIF has focused its private sector support for Chile in six areas: (a) expanding private sector activities, especially in transport and energy sectors, (b) stimulating global integration of the Chilean economy, (c) creating dispute settle mechanisms, (d) improving human resources productivity, (e) strengthening environmental regulations, and (f) developing small enterprises by providing access to financial and business services. From 1996 to1999, the MIF provided funding to strengthen the National Environmental Commission through staff training in rules and standards. It also financed three successful labor initiatives with programs to develop the technical skills of low-income youth, provide occupational training for youth with disabilities, and certify the skills of employees and workers. In the coming years, in light of the government's priorities and the Bank's strategy, the Fund's efforts will focus on promoting Chile's competitiveness and integration into the new economy and on improving the state's management and its relationship with civil society. For 2000-02, MIF's program of operation includes 9 projects, totaling US$ 8,34 million. One of two projects already approved involves the financing of a microenterprise expansion plan (US$ 570 thousand). The remaining 6 operations focus in sectors such as regulation of electronic commerce, public transportation, and small and medium size businesses.

Tables

Table 1: Net Resource Flows to the Emerging Market Economies

	1980-89 (Annual Average)	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Total	**41.7**	**60.4**	**78.2**	**108.6**	**171.9**	**170.5**	**212.3**	**256.0**	**280.5**	**265.5**	**214.9**
Official Flows	11.7	21.1	23.7	17.8	17.7	11.1	22.1	0.9	15.2	24.0	16.6
MDB Flows	5.96	7.72	6.25	3.94	6.19	2.15	3.98	4.03	13.69	14.84	12.32
Composition											
IBRD	3.61	4.49	2.71	-0.22	2.66	-0.53	0.58	0.99	6.58	6.84	4.29
IDA	1.03	1.13	1.43	1.81	1.33	1.41	1.28	1.44	1.24	1.10	1.00
RDB Concessional*	0.07	0.20	0.04	0.03	0.09	0.04	0.04	0.01	0.02	-0.03	0.03
RDB Non-Concessional*	1.25	1.90	2.07	2.31	2.10	1.23	2.08	1.59	5.85	6.92	7.00
Private Flows[a]	30.0	39.3	54.5	90.8	154.2	159.4	190.1	255.1	265.3	241.5	198.3
Net flows on debt to private creditors	20.2	17.4	19.1	38.0	47.1	49.8	61.7	95.4	90.5	80.9	2.5
FDI	9.4	19.2	28.6	39.3	56.5	77.4	94.7	114.4	147.4	146.1	162.4
Portfolio equity flows	0.4	2.8	6.8	13.4	50.6	32.2	33.7	45.2	27.3	14.6	33.4

[a] Private net resource flows are defined the sum of net flows on debt to private creditors plus net direct foreign investment and portfolio equity flows. Net flows (or net lending or net disbursements) are disbursements minus principal repayments.
* Publicly guaranteed; does not include the EBRD.
Data sources: The World Bank, *Global Development Finance*, 2001; data on MDBs comes from The World Bank, *World Development Indicators,* 2000.

Table 2: Private sector financing commitments (millions of US $)

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
IFC commit*				1764	2412	2112	2402	2699	2800	3500
AfDB						20	48	146	127	…
ADB			203	51	174	263	119	199	153	…
EBRD**	9	458	1041	1127	1240	…	1852	1898	1622	…
IIC					145.7	198	310.8	556.2	634.6	511.8

Source: Annual Reports

Table 3: The Emerging Market Economies*

	$4000 +	$2500-$3999	< $2500
'Top Twenty' in both absolute and per capita net inflows of private capital (average 1995-1998)	Chile, Mexico, Korea, Poland, Hungary, Czech Rep Argentina, Brazil	Malaysia Venezuela	Colombia
'Top Twenty' in absolute net inflows of private capital.		South Africa Turkey	Thailand Russia, China, India, Indonesia, Philippines
'Top Twenty' in per capita net inflows of private capital	Croatia, Uruguay	Slovak Rep., Estonia Costa Rica, Panama, Lebanon,	Peru

Source: World Bank WDR 2000-2001; Annual per capita income is denoted by 1999 GNP per capita. See Table 5 for rankings.
* We include in this group only countries with a population greater than 3 million.

Table 4: MDB Vital Statistics	IBRD	IFC	IDB	IIC	AfDB [2]	ADB [2]	EBRD [3]
Authorized capital	188 220	2 374	100 881	703	22 375	48 456	19 641
Callable	-176 825	-24	-96 544		-19 610	-45 042	-14 478
Paid-in	11 395	2 350	4 338	2045	2 765	3 414	5 163
(paid-in/callable capital)	6.4%		4.5%		14.1%	7.6%	35.7%
Assets	230 808	33 456	64 355	361	12 864	41 653	19 595
of which:							
Loans Outstanding net of loans loss provisions	113 668	6 241	37 385	243	9 026	24 698	4 917
Liabilities	202 787	28 112	52 582	153	9 039	31 590	14 523
of which:							
Borrowings	115 739	12 429	39 553	150	7 582	23 744	12 562
Equity	28 021	5 334	11 774	118	3 825	10 063	5 072
Total Liabilities and Equity	230 808	33 456	64 355	361	12 864	41 653	19 595
Income	9 642	1 506	3 194	28	759	1 833	376
Expenses[1]	7 995	1 256	2 626	41	600	1 366	334
Operating Income	1 647	249	568	-13	158	467	43
Less contribution to special programs	-129	3	0	0	16	-34	0
Net Income	1 518	246	568	-13	142	464	43

Source: Financial Statements of the Institutions

1 Includes administrative expenses

2 1998 Financial Statement

3 In Euros

4 Appropriation of guarantee fees to special reserve

5 Corresponds to subscribed capital

Table: 5 The EMEs

Net Private Capital Flows 95-98 (Average 95-98)

Aggregate $US Billions		*Per Capita $USD*	
China	49.32	Chile	532.0
Brazil	36.43	Argentina	462.5
Mexico	21.00	Malaysia	456.6
Argentina	16.71	Hungary	417.7
Korea, Rep.	14.76	Czech Republic	371.2
Malaysia	10.13	Panama	352.5
Russian Federation	10.11	Korea, Rep.	317.9
Thailand	8.79	Croatia	317.5
Indonesia	8.70	Lebanon	255.3
Chile	7.89	Estonia	249.7
Poland	6.84	Brazil	219.6
India	6.13	Mexico	219.1
Colombia	6.11	Venezuela, RB	206.5
Turkey	6.04	Slovak Republic	199.1
Venezuela, RB	4.80	Poland	176.8
Hungary	4.22	Latvia	157.0
Philippines	4.07	Colombia	149.7
Czech Republic	3.82	Costa Rica	149.5
South Africa	3.76	Peru	148.5
Peru	3.68	Lithuania	146.7

The EMEs - 'Top Twenty' in either aggregate or per capita (population > 3 million)

Argentina	Philippines
Brazil	Poland
Chile	Russian Federation
China	Slovak Republic
Colombia	South Africa
Costa Rica	Thailand
Croatia	Turkey
Czech Republic	Venezuela, RB
Estonia	
Hungary	
India	
Indonesia	
Korea, Rep.	
Latvia	
Lebanon	
Lithuania	
Malaysia	
Mexico	
Panama	
Peru	

Table 6: MDB Financial flows to Middle Income Countries

Net financial flows, IBRD (millions of current $US)
Net financial flows are disbursements of loans and credits less repayments of principal.

	1990	1991	1992	1993	1994	1995	1996	1997	1998
Argentina	171.7	109.1	-211.4	1172.8	122.7	682.4	794.8	497.8	1678.4
Brazil	-468.5	-408.4	-684.7	-807.7	-705.6	-539.4	278.2	367.5	245
Chile	132.2	44.3	32.2	-65.2	-111.2	-621.4	-187.8	-24.7	-34.5
China	375.6	537.9	356.7	731.9	1065.5	1107.1	943	1210.8	1078
Colombia	-220.6	-190.6	-419.2	-294.4	-525.8	-176.4	-198.2	-248.1	-47.7
Costa Rica	-40	-12.6	-18.4	-37	-45.4	-39	-31.7	-34.2	-20.6
Croatia	..	..	..	-32.6	-28.1	29.4	88.9	100.4	91.5
Estonia	..	..	1.1	18.9	9.7	18	16.5	10.9	10.3
Hungary	160.5	262.3	192.8	84.6	-28.1	-63.2	-419	-32.8	-802.3
India	747.3	703.4	218.6	458.3	-85.6	-354.3	-154.4	-278.1	-307.4
Indonesia	436.4	790	326.6	430.4	-55.6	89.8	-503.1	-245.2	479.1
Korea, Rep.	-402.2	-331.2	-216.7	-205.8	-306.1	-316.6	-175.6	2797.9	2875
Lebanon	-6.5	-4.2	-4.6	17	22.5	47.1	27.1	31.5	38.4
Malaysia	40.7	24.3	-43.3	-12.9	-41.4	-106.3	-76.4	-75.1	208.4
Mexico	2524.4	627.7	370.5	107.3	-122.8	320.8	-358.7	-316.1	25.9
Philippines	205.8	44	220.7	332.8	-57.8	-20.5	17.7	-112.1	-94.8
Peru	0	-94.4	-94	401.1	90.7	116.4	29.3	425	207.1
Russian Federation	0	0	0.9	371.3	282.6	823.6	1097.1	2690.6	1160.3
Slovak Republic	0	66.6	43.6	39.8	85.6	7.7	6	-2.2	-1.7
South Africa	0	0	0	0	0	0	0	0	0
Uruguay	8.4	38.8	129.5	-8.7	-19.2	-46.1	-31.1	-17.5	65.3
Venezuela, RB	840	329.9	176.9	19.7	20.1	-69.1	-120.9	-81.3	8
Poland	54.1	349.3	342.8	317	672.3	191.3	266.3	83.6	-22.6
Thailand	-33.7	-46.8	-468.5	-20	-287	-55.5	-58.5	251	319.2
Turkey	6.2	-215.1	-441.9	-393.5	-457.2	-459.7	-325.9	-426.4	-365.8
Panama	-41.1	-49.2	-117.9	-53.9	-52.2	-40.1	37.1	24.7	65.1
Czech Republic	0	133.3	87.2	92.9	30	56.7	32.2	-16.7	-20.8
Total	4490.7	2708.4	-220.5	2664.1	-527.4	582.7	992.9	6581.2	6836.8

Net financial flows, IDA (current US$ Millions)

	1990	1991	1992	1993	1994	1995	1996	1997	1998
Chile	-0.7	-0.7	-0.7	-0.7	-0.7	-0.7	-0.7	-0.7	-0.7
China	506.9	611.3	776.8	865.1	671	798.2	790.6	687.1	553.8
Colombia	-0.7	-0.7	-0.7	-0.7	-0.7	-0.7	-0.7	-0.7	-0.7
Costa Rica	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2
India	647.7	812.1	1030.4	495.2	772.5	502.8	671.9	579.9	578.5
Indonesia	-11.2	-13.4	-15.3	-17.6	-19.9	-20.4	-20.4	-20.4	-21.1
Korea, Rep.	-2.4	-2.6	-3	-3.5	-3.5	-3.5	-3.5	-3.5	-3.5
Philippines	-1.1	31.9	33.1	0.5	2.9	8.1	13.1	7.6	6.5

Thailand	-1.2	-1.1	-1.1	-1.4	-1.7	-1.8	-1.8	-1.8	-2.3
Turkey	-4.2	-4.4	-5.3	-5.9	-5.9	-5.9	-5.9	-5.9	-5.9
Total	1132.9	1432.2	1814	1330.8	1413.8	1275.9	1442.4	1241.4	1104.4

Net financial flows, RDB concessional (current US$ Millions)*

	1990	1991	1992	1993	1994	1995	1996	1997	1998
Argentina	-1.88	-1.88	-1.88	-1.88	-1.88	-1.88	-1.88	-1.88	-1.88
Brazil	-5.50	-5.10	-5.11	0.10	-0.90	-0.90	-0.45	0.00	0.00
Chile	-1.31	-1.32	-1.33	-1.33	-1.22	-1.35	-1.33	-1.04	-1.04
Colombia	-7.60	-12.68	-12.59	-12.20	-10.44	-10.37	-12.02	-11.47	-12.21
Costa Rica	4.14	-9.16	-10.35	-10.63	-8.50	-11.16	-11.22	-10.17	-11.13
Indonesia	107.86	14.88	36.91	45.39	35.42	40.27	22.55	18.87	-1.30
Malaysia	-0.34	-0.41	-0.47	-0.56	-0.63	-0.39	0.00	0.00	0.00
Mexico	-12.61	-11.16	-9.83	-8.32	-6.97	-6.97	-5.93	-4.69	-2.76
Philippines	118.40	94.51	78.53	94.57	50.08	49.70	45.82	47.87	21.28
Peru	-0.04	-21.79	-13.38	-6.83	-7.21	-8.15	-7.17	-6.60	-6.60
Uruguay	1.86	5.61	3.52	-0.18	-1.05	-1.74	-1.73	-1.73	-1.73
Venezuela, RB	-3.28	-2.31	-1.34	-1.34	-1.34	-1.34	-1.34	-1.34	-1.34
Thailand	-0.73	-1.20	-1.60	-1.26	-1.45	-1.55	-1.40	-1.64	-1.63
Panama	-0.35	-8.06	-32.85	-7.56	-6.69	-5.60	-9.47	-8.83	-6.54
Total	198.62	39.92	28.23	87.98	37.23	38.60	14.43	17.34	-26.87

*Does not include the EBRD

Net financial flows, RDB nonconcessional* (current US$ Millions)

	1990	1991	1992	1993	1994	1995	1996	1997	1998
Argentina	296.149	248.66	-18	798.479	-32.128	706.708	174.21	554.735	66.88
Brazil	-13.116	-4.887	46.152	58.66	11.991	114.713	468.49	1015.84	1318.3
Chile	189.212	78.882	100.74	-39.263	-24.811	-1115	-403.04	-342.94	-42.82
China	52.909	167.62	166.28	352.989	464.321	511.048	653.28	495.582	621.98
Colombia	265.805	195.28	319.45	21.854	-177.59	-62.634	14.179	-145.21	149.78
Costa Rica	30.078	32.465	53.596	61.996	62.268	107.888	23.537	77.569	9.855
Estonia	..	0	0	3.25	6.173	12.7	26.579	-3.402	..
Hungary	0	0	11.417	17.182	21.716	109.98	17.29	-29.921	..
India	187.901	542.56	360.02	147.627	448.849	250.4	502.36	480.332	490.51
Indonesia	561.673	431.22	416.07	403.799	-6.132	361.164	-833.58	173.642	873.89
Korea, Rep.	-13.639	46.551	54.154	-35.423	-26.729	-34.967	-93.176	1938.52	1678.3
Malaysia	16.828	41.986	12.076	-302.85	2.624	-14.703	-21.697	24.165	0.961
Mexico	97.918	286.47	129.71	108.311	-11.864	641.048	764.85	240.892	290.34
Philippines	145.023	78.897	74.667	68.796	94.966	-67.968	27.218	90.988	152.5
Peru	2.92	-213.87	346.5	221.852	125.3	190.646	99.606	476.539	169.96
Russian Federation	0	0	0	0	8.5	31.9	85.9	38.1	..
Slovak Republic	0	0	0	0	49.301	83.046	14.696	-8.276	..
Uruguay	18.029	103.73	7.535	115.059	74.361	28.02	59.078	135.506	99.233
Venezuela, RB	194.316	209.28	409.9	80.057	30.385	146.893	-69.855	-12.941	440.34
Poland	..	..	..	..	..	..	..	..	..
Thailand	-135.6	-171.43	-81.284	35.106	114.111	14.929	35.121	532.581	493.16
Panama	0	-0.323	-94.565	-14.333	-17.009	54.051	61.184	115.291	110.42

Czech Republic	0	0	0	0.828	8.205	11.619	-20.977	0	..
Total	1896.41	2073.1	2314.4	2103.98	1226.81	2081.5	1585.3	5847.6	6923.6

*Does not include the EBRD

Table 7: Private capital flows, net total (billions of current $US)

	1990	1991	1992	1993	1994	1995	1996	1997	1998
Argentina	-0.20	2.90	5.99	12.69	11.12	9.96	18.90	19.08	18.90
Brazil	0.56	3.61	9.68	16.21	12.33	19.99	31.03	40.33	54.39
Chile	2.10	1.47	1.79	2.36	5.08	5.51	7.34	9.44	9.25
China	8.11	7.51	21.30	39.55	44.39	43.67	50.10	60.83	42.68
Colombia	0.34	0.19	0.72	2.12	4.05	3.36	7.58	9.87	3.63
Costa Rica	0.02	0.15	0.23	0.20	0.24	0.38	0.40	0.52	0.80
Croatia	..	..	..	0.11	0.21	0.27	1.29	2.50	1.67
Estonia	..	..	0.10	0.16	0.21	0.21	0.19	0.34	0.71
Hungary	-0.31	1.01	1.16	4.73	2.78	7.88	1.74	2.60	4.68
India	1.87	1.54	2.08	5.02	7.14	4.93	6.68	6.78	6.15
Indonesia	3.24	3.45	4.55	1.06	7.75	11.52	16.17	10.86	-3.76
Korea, Rep.	1.06	5.53	7.50	8.75	12.87	13.67	19.88	17.85	7.64
Lebanon	0.01	0.01	0.00	0.00	0.41	0.75	0.74	1.07	1.74
Malaysia	0.77	4.16	6.07	11.26	8.46	10.10	12.80	9.31	8.29
Mexico	8.25	12.15	9.23	21.25	20.71	15.94	25.11	19.77	23.19
Philippines	0.64	0.40	-0.77	3.27	3.87	4.31	4.99	4.41	2.59
Peru	0.06	-0.07	0.04	2.07	4.52	3.66	5.50	2.85	2.72
Russian Federation	5.56	0.47	9.33	2.05	0.58	1.21	7.44	12.43	19.35
Slovak Republic	0.28	0.10	-0.23	0.56	0.56	0.52	1.33	0.96	1.48
South Africa	..	..	..	..	2.08	7.04	2.10	5.10	0.78
Uruguay	-0.19	-0.14	0.15	0.20	0.34	0.34	0.47	0.60	0.50
Venezuela, RB	-0.13	2.17	1.54	0.96	0.14	1.01	4.59	6.73	6.87
Poland	0.07	0.54	0.72	2.16	1.24	5.06	5.33	7.30	9.65
Thailand	4.40	4.99	4.30	7.54	4.43	10.04	13.70	3.61	7.82
Turkey	1.78	1.07	4.45	7.27	1.64	2.32	7.97	12.22	1.64
Panama	0.13	0.03	0.22	0.14	0.49	0.30	0.47	1.67	1.46
Czech Republic	0.88	1.20	0.60	2.10	1.64	5.20	4.89	1.87	3.33
Total	39.30	54.42	90.75	153.82	159.27	189.13	258.72	270.90	238.15

Source: World Bank, *Global Development Finance 2001.*

Table 8: Pricing and Tenor of MDB Loans							
		IBRD		IDB[1]	AfDB	EBRD	ADB[1]
Loan Charges (LIBOR Based $US Single Currency Loan charges as of January 1, 2000)		Variable spread	Fixed spread				
	Contractual spread	75	80	50[2]	50	100	60[2]
	Benefit of Sub LIBOR[3] Funding Cost	-33	-25	-22	-5	-	-
	Waivers	-25	-25	-	-	-	-
	Net Spread over LIBOR (I)	**17**	**30**	**28**	**45**	**100**	**60**
	Commitment charge	75	85[4]	75	75	50	75[5]
	Waiver	-50	-50	-	-50	-	-
	Net Commitment Fee	25	35	75	25	50	75
	Spread Eqv. of Commitment Fee [6] (II)	**21**	**26**[7]	**63**	**21**	**42**	**32**
	Contractual Front-end Fee	100	100	100[8]	0	100	100
	Spread Eqv. of Front-end Fee[6] (III)	**26**	**26**	**23**	**0**	**26**	**26**
	Total Spread-Equivalent over LIBOR (I+II+III)	**64**	**82**	**114**	**66**	**168**	**118**
I.							
II. Typical Loan Tenor (years)							
	Maturity	**17**[9]			**20**	**5-10**[10]	**10-14**[11]
	Grace Period	**4**			**9**		**4**

Source: Loan charges from World Bank Financial Products and Services, http://www.worldbank.org/fps/newmdbtable.htm, loan tenor from Bank documentation.

[1] Only a small portion of USD lending by IABD and ADB is priced off USD LIBOR.
[2] This is a variable spread. The spread shown for ADB was changed as of January 1, 2000. The previous spread was 40 basis points.
[3] The IBRD average cost margin (sub-LIBOR spread) shown is for USD SCL rate settings from January 15, 2000 through July 15, 2000. Sub-LIBOR spreads for IADB and AfDB shown are the current sub LIBOR spreads for USD.
[4] For the first four years, an additional commitment charge risk premium of 10bp is charged on the undisbursed amount over and above the contractual commitment charge.
[5] The commitment charge is applicable to the following proportion of loan amount less the cumulative disbursements: 15% in the first year, 45% in the second year, 85% in the third year and 100% in the fourth year and beyond.
[6] Spread-equivalent computations for commitment charge and front-end fee use an average IBRD disbursement profile derived in FY99 using historical sector and instrument specific disbursement profiles. The profile so derived does not factor in events such as loan cancellations, prepayments and protracted debt service problems faced by the Bank. Typical repayment terms used are as follows: Final Maturity: 17 Years; Grace Period: 4 Years; Payment Term: Equal Payment of Principal. Disbursement profiles and payment terms vary across MDBs and hence spread-equivalent charges would vary based on the disbursement profile and payment terms used.
[7] To account for the commitment charge risk premium an average spread of 5 basis points was added to the normal commitment charge spread equivalent.
[8] The front-end fee is collected over a four-year time horizon: 25% in each year.
[9] The World Bank sets loan maturities according to three broad categories of 'low' 'middle' and 'high' income countries. Our set of emerging market economies falls in the World Bank's 'low' and 'middle' classification. For emerging market economies, World Bank loans are set with a maturity of 17 or 20 years and a grace period of 4-5 years. The World Bank offers 15-year loans with a 3-year grace period to 'high' income borrowers.
[10] Longer maturities may be considered on an exceptional basis, for example up to 15 years for infrastructure operations.
[11] The maturities of the loans extended by ADB are somewhat more flexible, ranging up to 30 years, including grace periods ranging up to eight years.

Table 9: IBRD Graduates

Full Graduates						
Country	Last Year Borrowed	Amount ($m) of last loan	Years without borrowing	Total borrowed ($m)		
France	1947	250	53	250		
Luxembourg	1948	12	52	12		
Netherlands	1957	15	43	244		
Belgium	1958	10	42	122		
Australia	1962	100	38	463.7		
Austria	1962	5	38	152.3		
Denmark	1964	25	36	85		
Norway	1964	25	36	145		
Italy	1965	100	35	399.6		
Japan	1967	100	33	862.9		
South Africa	1967	20	33	287.8		
Taiwan (PRC)	1971	70	29	329.4		
New Zealand	1972	8	28	126.8		
Iceland	1974	17	26	47.1		
Finland	1975	20	25	283.8		
Israel	1975	35	25	284.5		
Singapore	1975	25	25	181.3		
Ireland	1977	71	23	223.5		
Spain	1977	18	23	478.7		
Greece	1979	25	21	419.8		
Portugal	1989	90	11	1338.8		
Slovak Republic	1994	135	6	285		
Graduates that have returned to borrowing status						
Country	Last Year Borrowed (before relapse)	Amount ($m) of last loan (before relapse)	Year of re-initiated borrowing	Total amount borrowed since re-initiation ($m)	Years without borrowing	Total borrowed ($m)
Costa Rica	1994	22	2000	32.6	5 (1995-99)	921.5
Malaysia	1994	120	1998	704	5 (1995-99)	4150.6
Korea	1995	275	1998	7048	3 (1996-98)	15,647
Chile	1996	15	1999	160.6	3 (1997-99)	3586.1

Source: World Bank, 2000. All data refers to Bank commitments.

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