CARNEGIE ENDOWMENT FOR INTERNATIONAL PEACE

"VOLCKER/GURRIA COMMISSION URGES WORLD BANK NOT TO END FINANCING FOR MIDDLE-COME COUNTRIES"

Carnegie Endowment for International Peace
Washington, D.C.
April 26, 2001
12:40 PM

Transcript by:
Federal News Service
Washington, D.C.

MS. BIRDSALL: I'm Nancy Birdsall. I'm a senior associate here at the Carnegie Endowment for International Peace, and I'm pleased to welcome all of you. On behalf of the co-sponsors with the Carnegie Endowment of this report, and the co-sponsors are the Inter-American Dialogue and Emerging Market Economies Financial Advisers, I am welcoming you.

We are here to talk about a report that is now being released. I think you have the press release on the role of the multilateral development bank in emerging market economies. This is the outcome of a commission of 33 distinguished people, chaired by Jose Angel Gurria, on my left, and by Paul Volcker, who cannot be with us today.

Why did we put together this commission, the Carnegie Endowment and our co-sponsors? We did it essentially because the questions have been in the air now for at least a year, maybe longer. Why should the multilateral banks be lending to countries that have access to private capital markets at the same time that the poorest countries who don't have access to capital markets seem to be in such great need. So you know we could get relief discussions focused heavily on Africa, with the recent concerns about the spread of the HIV virus, with the question of the rescues for emerging market economies, all that has been in the air.

In particular, about a year ago there was a report that was mandated by the US Congress, an international financial advisory group chaired by Alan Meltzer at Carnegie-Mellon University, which is different from the Carnegie Endowment for International Peace. In the Meltzer report there was discussion of this very question. The group, the majority group of the Meltzer commission recommended that the banks desist from lending to countries who had reached certain levels per capita income, or who had achieved an investment grade rating.

So that is the background for our putting together the commission. I'm going to ask Angel Gurria to tell you a little bit about the commission's deliberations and conclusions and recommendations. Most of you will know that Angel Gurria is from Mexico. He was the minister of foreign affairs in the Zedillo administration, and after that the minister of finance. He had a distinguished record before being – having the double ministries, you might say, the double whammy, in Mexico. He's seen it all and certainly has thought a lot about the role of the multilateral institution in Mexico and elsewhere as well.

MR. GURRIA: Thank you, Nancy. First of all, it is an excellent opportunity to express the appreciation of the co-chairs, Paul Volcker and myself, for the work of the commission. We have Carmen Reinhart and John Williamson here. We have two very salient examples of the very high quality and the dedication and the caliber of the people who worked. We had people literally from all over the world, from Africa, from Asia, from Latin America. Some veterans from all these institutions, from the world of academia and certainly very high quality inputs that allowed us to put together the report.

MS. BIRDSALL: And from the private sector.

MR. GURRIA: Yes, indeed. The private sector, from banks, from investment banks and from think tanks. So we had a very, very complete – I think in the press release you have the names of people there. That's something which I think is important.

MS. BIRDSALL: The list is in the report.

MR. GURRIA: The second, having done that, I'd like to say that it has been a source of concern, and certainly this started when I was still the minister of finance, but we could not become an independent panel of experts, and that was something that the Carnegie Endowment for International Peace, when they called us, Paul Volcker and I, to co-chair this group, we accepted immediately because we were aware of the discussion that is going on.

In fact, I am going to present the recommendations and the conclusions of the study a little later today in an event organized by American University, Colin Bradford. And tomorrow is a forum of the Bretton Woods Committee. We have an early slot there, about 9:30 in the morning, to present again to the very distinguished audience the conclusions of this study because we think it is of great consequence and it's an important contribution to the discussion today.

It is no less than the question of whether these institutions should continue for practical purposes to exist in the way in which we know them. Because the idea that they should stop lending to countries, like mine, like Argentina, to speak of a country where the importance of these institutions today acquires enormous relevance, to the Colombia of a few months ago that was having problems in order to roll over the refinancing of their debt, and of course to the Turkeys and the Brazils, and clearly to the Indias and Chinas of this world. Meaning, to those countries where because of enlightened economic policy or because of the size of their economy, the market today has given access.

Many of these countries, if not all, at some point in time either have or have maintained, and sometimes on and off, access to markets. And the question then was, should those countries where there is market access be the beneficiaries of the action of the multilateral development banks. And I want to start by saying, we come out with a very conclusive, very strong yes, they should. The message should be loud and clear, it is unequivocal, there should be continued lending to emerging market economies by multilateral development banks all over the world.

There are many reasons why this should be, but I would like to just, in broad brush strokes, elaborate on some of the more important, being that the markets are quite imperfect. Anybody who suggests that because there is market access then the countries don't need anything else is forgetting not only history but even the very, very recent events. It's forgetting the fact that when there was a crisis in Russia, for example, it hit Latin America, and the market closed down for the whole of the emerging markets in the developing countries, as did Russia, where the most important trading partners, or as if Russia were next door to each one of us.

You couldn't get a loan for Brazil or Mexico, even less so to the private sector of Mexico or Brazil or Argentina or Thailand or Korea because of Russia. Even more so when the problems are closer to home, like they are today in the tensions that we are living every day in the Argentinean case, and as I mentioned before, in some other cases in the recent past.

It is not that the international financial institutions, it is not that the multilateral development banks are going to substitute for the totality of the float. If anything, the question of should these institutions continue to lend to these countries was posed because of the relative size of the contribution of these institutions, which is now probably around the 20th or one 15th of the total flows that the private sector provides to these countries. At some point in time the flows were about 80 times what the institutions provided because typically when the going is good, we see these flows moving into the country. Then of course the need posed to the multilateral are smaller. They are needed less, and at the same time the amounts become smaller.

Ah, but it is precisely when things start getting a little rocky, start getting a little difficult, when the enormous importance of these institutions becomes more evident, because you have a counter-cyclical contribution and because the role of these institutions is to continue to promote development and to continue the welfare of these societies, regardless of what the markets are looking like. Or what the spreads may be in launching a new bond issue for a particular country. And even more so when you have absolute closure in extreme situations where, as I said, nobody can launch at any price. Because the fact that Argentinean bonds today may be quoted at 10 over the Treasury means simply that you can't launch a new issue at 10 over Treasury. It simply means that the perceived risk of the region as a whole today is going through a period of stress and tension.

Therefore, these institutions play a very important role. They play a very important role because they give an imprimatur of quality to the economic policies of these countries. By supporting the policies and by supporting the project, they are saying to the rest of the world, these are good quality policies, these are good quality projects. At the same time they complement, even in the absence of pricing. That is very important.

Again, people tend to think in extreme terms, either in crisis, absolute crisis, or in terms of total normality. In one case they are absolutely needed. In the other case they are not needed at all. The world most of the time is some place in between. In Latin America, typically, most of the time it's some place in between. Meaning we cannot say they are perfect institutions, they work very well, we're so happy, we're so satisfied. That is not the case. Clearly these institutions are needed, but we also need to question, we also need to comment, we also need to analyze what it is that they do, how they do it, when they do it, and the different modalities in which they interact with these emerging market economies.

They also provide a service which is of interest, and that is not analytically obvious. And that is, if a particular country, even in the good times, has to make a refinancing effort of, say, five, six, seven billion dollars a year, but of that the World Bank together with the IDB, or if it's an Asian country, the World Bank together with the Asian Development Bank, can provide a couple of billion. That's a couple of billion times in which you don't have to go to the market. That means even in the good times a country will go to the market for three, four, five billion dollars, and then not be seen as refinancing the rest of its requirement because it is doing so through the international or multilateral development institutions.

Therefore, the conditions that it will get for the first $5 billion where it does have to go to the market are better because it will be coming less to the well. And the less you come to the well, the better off the market will receive you, the better off you will be.

Now, there's also a question of whether the institutions could do a lot of good without necessarily lending. And the conclusion that we got to is that technical advice, technical assistance by these institutions is of critical importance as a policy input in all these countries, but that it is the lending part of the institutions that functions as the transmission belt, and that the only thing that makes them different than any adviser who can come in and give you advice on how to do good economic policy is that they come with a half a billion dollars under their arms, or a billion dollars, and that that causes a policy discussion on either the agricultural sector or the infrastructure sector or the water sector, or on foreign trade policies, on the policies of liberalization, or the new areas of policy, judicial reform, security, the question of the digital divide and how we cover that gap, and forget about developing countries, how you avoid the digital divide from getting wider in developing countries themselves, within the borders of each one of the developing countries.

These are the real issues in which institutions like the IDB and the World Bank and the African Development Bank and the Asian Development Bank, and then some of the smaller institutions like Cabe (ph) Banco Centroamericano Economica, or COF (ph), or other subregional institutions are working and can contribute.

So I think again the message there is, yes, but the difference between anybody who can give enlightened technical advice and these institutions is that by providing a policy discussion forum around the granting of loans, there is a discussion of the quality of the policies overall that is very good for the countries, and that actually in many cases is sought by the countries precisely as a way in which people responsible for economic policy can focus on the different areas and on the quality of the policies of the different areas. Meaning that a minister of finance, a minister of planning would probably call in the people like the IDB or the World Bank so that through a loan questions like social security or the issues that you mentioned a while ago are discussed. In that sense again, the transmission belt of lending becomes very, very critical.

Now does this mean that we are complacent and that we would not propose any changes? No. The paper actually is very suggestive and very rich, and I think very generous in terms of the areas where proposals are made that could address some of the things that these institutions could do better. One of them, by the way, with a longstanding discussion, is whether at some point in time these institutions should stop borrowing from – or should stop lending to emerging markets. The Meltzer Report, for example, was suggesting automaticity. It said after $4,000.

This is another very distinguished member of our panel, of our group, Moises Naim former minister in Venezuela and now the editor of "Foreign Policy" magazine is sneaking in there. Come in.

The conclusion of the group here is, we should leave it to each one of the countries. After all, this is a cooperative. These are institutions in which we're all members. We're all shareholders. Ultimately we share the risk of their operations, not only ours but also of the others. And we therefore have the right to participate in these institutions whenever we deem that it is appropriate.

So the question really is a recommendation about self-graduation rather than a particular amount that would make for a mechanical conclusion, say after X. Because it really assumed that a country for a while has a very rigid or very strong exchange rate, for example. They would probably go over the minimum expressed in dollars very fast. No country would be the same.

We even went into the details, say, yes, but we should not penalize countries that at some point in time may have been successful. But what if they choose to come back again? Because sometimes countries do very well. They go to the markets, they don't think they need these multilaterals, but at some point in time they may get in trouble. Well, they of course have the right to come back. We even discussed similar things in the Annex. We discussed some of the things that could be done in order to make sure that they retain the right, regardless of whether they are at $4,000 or $5,000 or $6,000 per capita. The natural, the organic, the logical thing is to have a sort of a self-graduation policy, and some countries will adopt it earlier than others, depending on their mix. And also, depending on the stock of debt that they already have in these institutions.

History does not start today. They already have a history of borrowing from these institutions in the last 20 or 30 years, and therefore the refinancing requirements with these institutions will dictate how they get or how they liaise with these institutions themselves.

There's also a question, and this has been a word that has been used around Washington when discussing these issues very often the question of transparency. But it is linked today with a concern that was raised by the commission, in which we have also NGO's, of the question of the ownership, the relevant and the political support that adjustment or sectorial programs may have within the country. And the recommendation there is for the greatest possible degree of openness and transparency, meaning that all interested parties should be able to opine on particular policy changes or reforms as they are being discussed, and that eventually once a deal is struck and a policy is agreed upon, that the details of the commitments could be made public.

Now this of course does not mean that the commission is suggesting that everybody opine about anything that moves or anything under the sun. It is not an indication to open up every one of the issues to everyone who thinks they have something to say. Clearly here there is a question of representation, and there is also – I mean, on the one hand you want openness, transparency, and democracy, and on the other you don't want anarchy. You want to have an orderly discussion of issues.

But the question is, the issues that are more broadly discussed will then, when a conclusion is arrived at, not only by an particular official in the government, or by a particular member of the government, or even by a particular member of Congress, but by society at large, will enjoy much greater support and, therefore, will have a greater chance of being successful when it is put in practice. Then that in and of itself would be a very important element in the effectiveness of these institutions because there has been criticism in these institutions, or about these institutions in terms of how effective, how successful they may have been and their programs.

Clearly one of the ways in which we can, going forward, make sure that there be greater success is precisely the fact that the policies enjoy a broader support. And for that the question of transparency, public debate is very important.

Now there was also a question of saying the word subsidy was at times used in this discussion because there is a subsidy by these institutions to emerging market economies, and we came to the conclusion that there wasn't any subsidy in the sense of nobody is paying anything to anybody, but that we have created a very interesting, quite positive and quite effective system, without putting a lot of money on the table. The IDB, after all, is worth $100 billion in capital. The World Bank is $188 billion in capital. But the countries only need to put up a few billion dollars altogether, and the rest is callable capital. The rest is contingent upon the very remote possibility, never been used, that there would be a call on all the liabilities of these institutions. That at some point in time there was a sort of a subsidy. We all concluded, no, the thing is that we got a good thing going, that works well.

From the founding fathers, they developed a good concept where the contingency lies with the stronger members of the community and therefore that allows for these institutions to borrow at relatively cheap rates and pass on the money at relatively cheap rates to the countries, to the beneficiaries. And we have a good format, and that if something is working well, we shouldn't attempt to mess with it or to change it.

However, we have institutions like the Andean Corporation, La CAF, that work very well where there are no US, no Germanys, no Spains, no UK's, et cetera. There are only Andean countries, none of which have an investment grade rating today, and La CAF is investment grade. So again, it suggests that we could try formally going forward, different than the ones we have today on the table to solve particular issues if we need to strengthen the flows to emerging market economies.

There are some suggestions about how maybe pricing could be different, depending on the products, depending on the countries. I'm sure that's going to be somewhat controversial and will give rise to a lot of discussion going forward. But more generally, I would say the central questions that were raised left no doubt in terms of where we should be, in terms of why these institutions should continue to play a central role, probably even an increasing role, and things like regional or global focus goods. How does one deal with an outbreak of – forget about HIV and AIDS, which is now almost a classic problem because we've been dealing with it so long. You have outbreaks in the most developed countries in the world of hoof and mouth disease, or BSE, for example. How does one deal with situations like that in middle income countries in Africa or in Asia or in Latin America? You need institutions which are geared toward the region.

How does one strengthen the forces of integration, not just of Latin America as a region, or Asia as a region, or Africa as a region, but with, in our case, a hemisphere. There was just this meeting in Quebec. And how does one apply the strength, the power, the capacity, the capital of the World Bank and the IDB together to promote the process? How does one deal with the private sector?

Today many of the countries have a lot of limitations in terms of budgets. We're all moving toward lower budgets or no budgets or balanced budgets, and therefore, you can't use a lot of investments, you can't choose a lot of expenditure. But at the same time there are these market realities where the institutions need to be supported by MDB's, and at the same time you have new problems, new challenges. It's no longer just a dam, just a school, just a road, but these quality problems of cohesion, social cohesion within societies which are totally new, but which we're facing together. More and more with regional and trade integration you are facing the problems of your neighbor also, not only yours.

Again, the conclusion is, this makes the role of these institutions ever more important. So Nancy is telling me to open up for questions at this moment, and I'll take her cue and we will do so. Thank you very much.

MS. BIRDSALL: I want to make a quick point before we go to questions. We have an important mistake in the press release, which John Williamson has kindly pointed out to me. The fourth bullet should read, "Lending to emerging markets does not reduce" –

MR. GURRIA: Ah, yes, that is a critical issue. A bit of a problem. A little bit of a mistake. Let me just make one comment here so that you understand why this is of critical importance. It has been said often that because they had to lend to Mexico, Brazil, Indonesia or Korea, they're not going to be able to lend to Rwanda or to Haiti, or to Nicaragua and Honduras, or to the smaller, poorer countries. This is not the case. There is no crowding out. There is no insufficiency of resources.

The institutions are financially equipped in fact with a concept which is a sustaining level of lending, sustainable level of lending, which was developed in the case of the IDB's since the seventh replenishment at Amsterdam and then confirmed at the eighth replenishment at Guadalajara. And the World Bank has come to that level also. That means they can maintain their cruising speed.

The problem is today they are not lending. One practical issue and then I will again stop with this, is, imagine the World Bank and the IDB and the ADB and the AFDB without being able to lend to the middle income countries. Where would they get the net revenues that then result in the capacity to forgive debt to the poor, the most needy? Where do you get literally the profits? Where do you get the net income, as they call it? They don't call it revenues because – they call it profits because they are maybe a little embarrassed to call it profit if you're talking about a development institution. But where do you get that extra on top of what it costs to fund these institutions, that would then allow the special programs not to charge the technical assistance to these countries, et cetera? Where would they be? They would just become a black box of grants.

Today the world does not seem to be in a very generous mood. Politically it's very difficult to get countries to provide grants. So what we have is these institutions that through an accumulation of net revenue over time and their own original capital, they now provide these services in lieu of aid to the poorest countries. That's another very important consideration of why their continuous presence should be assured.

MS. BIRDSALL: Okay, let me make one other point before we turn to questions. On May 1st, Tuesday, we will have a presentation of the report with Paul Volcker and Mr. Gurria, at 12:30 at the Willard. If you would like an invitation and you have not received one, would you please contact the press office here at Carnegie and we will issue an invitation. That will be a public event and it will be on the record and you will be on live Web site, live audio.

We have in the press release and in the report itself which you have gone through, some of the issues in a much more terse way, perhaps too terse, than on how Nathan gave them to you. So I think the best thing is to open it up to your questions. Carmen and John as well as I would be happy to address questions.

Q Just a couple of things. At one point you said that the problem today is that the volume of lending is decreasing. Why is that?

MR. GURRIA: The volume of lending of the World Bank, the IDB, the ADB, the Asian Development Bank, has been dropping, and the reason is that if you have countries which have budget constraints, typically public programs get reduced or deferred, and allow the inertia of expenditure to take over, but then new programs, which are typically the programs financed by these institutions don't disburse, and in some cases even you have situations where ongoing programs are either reduced or deferred or stopped.

On the other hand, it is paradoxical that when you have a very good market period, several years, here you're talking about several years, which we have not had certainly because we've had problems in '97, '98, '99, and then the year 2000. But when you have better situations, the market tends to take care of more, of a greater proportion of the total needs.

Then when you crisis, then you have an increase in the amounts that the institutions provide because you have these large packages. You have Thailand, Indonesia, with $40 billion, $50 billion each, Korea, et cetera. Because we have had a relatively good market period, and at the same time because of the budgetary restrictions – and third, because in many cases this question of graduation should come naturally. Meaning, what is the difference between borrowing in the market and borrowing with the IDB or the World Bank? It's not just a question of cost. It also means that if you are market-worthy, you can go and put out a bond issue, the bond will be sold to investors, and investors will not ask what you're going to do with it. Whereas it takes six months to a year to negotiate with the IDB and the World Bank. A loan either of $50 million or $500 million, for that matter, doesn't make that much of a difference.

So at some point in time the graduation process means the country's opting out of that and saying, My God, you now, to get the last $500 million, if it's only money that we're after, there are many other ways to get it. But basically you're never only after money when you're dealing with the multilateral development banks.

MS. BIRDSALL: I think it's important to clarify a little bit the issue of the level of the lack of funding. What has happened is that in the World Bank in particular, which has been the more mature of the – it has the longest history. If you look only at the traditional investment loans, if you exclude the privatized loans that went out in '98 and that went earlier to Mexico and Argentina in '94, '95, if you exclude those loans, the trend in the normal bread and butter investment lending of the World Bank is level.

MR. GURRIA: It's what you call investment loans.

MS. BIRDSALL: And there were two issues that are on the table. One is that many of the emerging market economies that we're talking about here have moved far left as they move toward graduation. The other is, and we discussed this briefly in the report, some of the poorer countries that borrow are constrained not by availability of capital in the bank. That is not the issue. They're constrained by policy shortcomings, or by an inability to absorb because of administrative or institutional constraints, more lending.

So this is all part of a general picture which says, there is no opportunity cost to the poorer countries when the multilateral banks lend to the relatively better off countries, such as Mexico, Turkey, Malaysia, Thailand, and so on.

MR. GURRIA: There's no crowding out.

Q Mr. Gurria, what are your thoughts on the potential Argentine default?

MR. GURRIA: Well, first of all I'm going to start by assuming there won't be one. But one of the reasons why we may not have one is precisely because the institutional setup has improved enormously since the Mexican crisis. Very frankly, putting together a $50 billion package in 1994 and '95 is something we all thought was never going to be repeated again, was not do-able, and it had to be done for Korea, for Indonesia, for Thailand, etc.

But the experience, if anything, has been good because you have had recovery, you have had stability, and yes, the stability of Brazil is good for all the world, the stability of Mexico is good for all the world, that of Argentina and that of Thailand and Korea is good for all.

Now, take the opposite view, the opposite situation. You say these institutions are not going to participate. Then how is it, even if you think about bilateral support, think about the US participation, or in some cases in Asia, the Japanese participation, and some cases in Africa, the European participation to support some of the countries that may face trouble. The institutions not only provide money. They provide the framework in which the recovery programs are set. That is very, very important.

I should say that if these are called multilateral development banks, the ultimate challenge is to find ways in which they can promote development, and getting countries out of crises, or, even better, preventing countries from getting into a crisis, is a very, very important development goal.

Q: I just wanted to make a comment. I think in this report it clearly comes out that lending to the middle income emerging markets. I mean there is no crowding out issue. And I think the word we have not yet mentioned is the word contagion. The prospects for having contagion affect poor and middle income alike is far greater when the middle income economy gets into trouble and into crisis than when a poor country that never had access to capital markets gets into trouble.

So, in effect, one of the reasons why I think lending to middle income countries is justified is the whole issue, notwithstanding that there are -- yes, there're moral hazard and all that -- but that contagion is alive and well. And it hurts the middle income and it hurts the poor. And contagion is most likely when a middle income country like Mexico, like Taiwan, gets into crisis. And let me just conclude my comment by saying that let's also think about what middle income means. You know, we tend to think of middle income as this sort of, you know, middle class, nice, comfortable. No, it's not.

I mean the gap between middle income and high income is vast. Vast. And so we're classifying them as middle income because they're somewhere in the middle, right. But not because there's any lack of gap. There's a very wide gap between what we classify as high income countries and middle income countries. And a lot of the poverty problems, the environmental problems, all the problems that you can think of are alive and well in that middle income category.

MR. GURRIA: Carmen's point is excellent. Let me just give you a numbers illustration of what she just said. There is this criticism that 80 percent of the money of these institutions goes to 11 countries. It happens to be that those 11 countries have 80 percent of the world's population and also 80 percent of the world's poor. It is very important. In China, in India, but also in Mexico, because we have 100 million people but 40 million are in poverty, 20-odd million are in extreme poverty. These are well-known numbers. And the same with Brazil and the same with Argentina. The larger the population in the developing countries, there is a very important number of people who are in poverty.

So as Carmen said, we are not talking about the upper middle classes of the middle income countries as they are called. We are talking about the capacity of these institutions to continue to work in these countries because the poor are there. That is where the greater number of poor people are.

MS. BIRDSALL: I'd like to make an additional point about the current situation in Washington, and one reason why your question about Argentina is important. The conditions recommendations for crisis lending are very clear, that it is, as Angel said, a kind of development lending. In part because the poor suffer within countries, and in part because this contagion affects developments in other countries besides the one that may be hit at a particular moment in time.

The message is said in a specific context, however. Names that the banks should not substitute for IMF style, or IMF type crisis lending, that when the banks enter in, it should be with a medium-term development purpose. It should be associated with initiating or protecting programs that deal with the financial sector, or with the social –

MR. GURRIA: Or social programs.

MS. BIRDSALL: -- that protect people in these kinds of crises. One of the reasons the question is important is that there is still today some uncertainty in

Washington about how the Bush administration will handle these crises should they occur, and that has been true for Turkey, for Argentina. The views of the commission on crisis lending I hope are clear.

[TAPE CHANGE.]

MR. GURRIA: -- through lost jobs and lost income and interrupted education for children, et cetera. Assisting countries to cope with crises helps alleviate poverty and therefore constitutes development lending. I would say a very important modality of development lending.

MS. BIRDSALL: We only have about 10 more minutes. We'll try to give shorter answers and take more questions.

Q: [Inaudible.]

MR. GURRIA: Well, first of all, in terms of what I would call the preconditions, and then the ongoing conditions for lending, that is a different concept because we have there a chapter, and we didn't mention them all, on the question of conditionality. The question that at some point in time we believe conditionality should be streamlined and simplified. Today you could literally have dozens and dozens of conditions for a particular loan. It should be easier to identify the critical issues.

However, the institution should be ready to enforce the conditionality to a greater extent, eventually even to stop lending in the face of either institutional or sector-specific conditions that are not being met. In that sense I think your point is very important.

Now also I think we should avoid the panacea syndrome. And here I include the IMF, the World Bank, the IDB, the multilateral development banks. They cannot do what governments, societies, congresses, and chief executives and members of a government don't want to do. That means in the end if a particular country does not want to work with these institutions under these rules, it is their privilege. The question is, these institutions should not work with countries that do not comply with these sorts of conditionalities, or with the overall behavioral framework, I would call it. So it literally takes two to tango.

Here it should be very clear what the conditions are, and then the enforceability and actual enforcement of these conditions, and compliance with these conditions, including the stopping of lending, is something that we make very clear.

Sorry. The second question was about?

Q Bailouts.

MR. GURRIA: Ah, the bailout. Yes, the bailout. Well, Nancy said the MDB should not be considered as an adjunct to the IMF simply to make a certain amount, total amount possible because you need $30 billion and the IMF can only make 17, so we get the other 13 out of the World Bank or the IDB or something like that. This is not the way in which we think these institutions should be considered.

However, as is said here, number one, to prevent crises, there should be a mechanism that is agile and where these institutions have ways of precommitting to support in different instances which are not of their own making. Like volatility, instability coming from, you know, third parties or whatever, third markets.

And the other thing is that I think experience shows that in the end when things came to a crunch, it was the private sector that paid for the difference. The last big round of middle income country debt reductions came from the private sector mostly. The World Bank and the IMF and the IDB have collected in full.

Now, it is also important to say the net income from which the HIPIC is being funded at the IMF, at the World Bank, and at the IDB and the other developing institutions is from the loans of middle income countries that are paying back to them in full because we can. Therefore there is, in a way, already in practice a call subsidy of the middle income countries in favor of the lower income countries, meaning a south-south type of cooperation because the allocation of the net proceeds over time has allowed a 40 percent, 50 percent, 60 percent reduction in net present value of the debts of the poorest countries of the world.

MS. BIRDSALL: I think on the question of bailing out the private sector, it really is important to maintain a distinction between the IMF and the banks in the following sense, that if the banks are doing lending into a crisis, it should be associated with a development effort. In terms of the mechanics, that is likely to mean that that lending is associated with fiscal expenditures for social programs, or with specific efforts in the financial sector to deal with the banking crisis.

This is very different from IMF resources that are fundamentally going into the central bank or going to build up confidence.

MR. GURRIA: Balance of payments.

MS. BIRDSALL: I mean, we can’t over-do it. Money is fungible. So the total amount matters. But when you consider that the total amounts from the banks are relatively small and have been during crises, and that they are tied to specific efforts, internal domestic efforts to deal with the medium term problems which have been associated with the crisis itself, it’s important to keep that distinction in mind.

Q -- In the case of Argentina, one of the things -- the amount of debt that is involved. And my question is do you think that the debt restructuring could -- ?

MS. BIRDSALL: Certainly that has been in the last couple of years –

MR. GURRIA: That's not new.

MS. BIRDSALL: It's not new. That has been the position.

MR. GURRIA: No. Well, actually, not only a couple of years. The first time that a restructuring, and in fact a reduction of the absolute size of the debt appeared as a condition of the IMF to support a particular country was with Mexico, where it was a very dramatic change. It signified the change between the Baker plan, which was, let's lend a lot of public monies to the government so that they continue to pay to the bank. They only ask from the banks that they continue a little bit of lending. The banks didn't even do that minimum.

So there was a big change. The sentiment in the US government and in the G-7 governments was dramatically changed and they said, no more. We are no longer going to give public monies to the countries so that they continue to pay the banks if the banks are not willing to make an effort. In fact, the net transfer of resources is so negative that we will never see growth from the highly indebted middle income countries of those days, mostly in Latin America, if there is no reduction.

So what the IMF did in the case of Mexico is they put a clause that said that debt reduction was a condition. Now the banks did not appreciate it very much in those days, but in the end it happened, as you know. And it happened also for Argentina and it happened for Brazil.

Q   [Inaudible.]

MR. GURRIA: What I mean is that this is a concept which has been now ongoing for a long time. It's not a new concept.

MS. BIRDSALL: And in Ecuador a year or two ago. The official institutions basically refused to, you could say, bail out the private sectors, Peru, Ecuador. So I think one point, what we see happening is in effect a kind of case by case approach. It seems to depend on the country, it seems to depend on the risk of contagion. It may depend on --

MR. GURRIA: And also the mix of how much you owe to the institutions and how much you owe to the market. That's very important also. That's very critical.

MS. BIRDSALL: I don't think we can expect to see a sort of despositive view on this issue ever emerge because the countries that can be helpful, such as the US, are likely to want to treat these issues case by case.

Q: -- Why do you think it's important to come out now with this report. What threat do you see, what real threats do you think are out there that would lead you to [inaudible]?

MS. BIRDSALL: Maybe I can take that question. I think in particular in the US context we say it's a situation where historically it is the administration, the executive branch of government that has taken the initiative in providing some kind of positive support for international institutions in general. That was true in the Bush administration, of Bush, Sr., which took many initiatives to provide leadership as a shareholder, as a member and shareholder in the World Bank and the other international institutions.

It has never been Congress that has been particularly interested in or helpful. Some members of Congress have always been knowledgeable about these issues, but as an institution the Congress in the US has generally been somewhere between apathetic and negative, vaguely negative on US participation and US support of these international financial institutions.

For that reason, it is important right now to get a sense of what this new Bush administration decides, the decisions it makes in the next year, the policy stance it takes on a range of issues that affect the multilateral banks is very important, and that is one of the reasons why I think this is a good moment for this commission to be putting out what we view as a very careful, balanced report. It is not ideological either in one direction or the other. It has the strong recommendation that the banks continue to lend to these countries. It also has, as Angel said, recommendations for ways in which the banks need to change in order to adapt to a changing environment.

In particular I should mention, because we haven't – well, only briefly. There is a recommendation that all of the banks put more attention to lending to the private sector and look at the policies that they have that make it either difficult or unlikely that they'll do the kind of direct lending to the private sector that should be catalytic, that should not substitute for lending by private banks or private creditors, but should be catalytic in drawing in additional resources to these middle income countries which are after all, though middle income, still relatively poor.

MR. GURRIA: This brings back to Gloria's original question. Why are they lending less. Well, which were the big ticket loans? Dams, thermoelectric plants, some types of major infrastructure. What is happening? Those are now being done by the private sector. The World Bank and the IDB cannot lend to the private sector. Their charters do not allow them to. The IDB actually can lend five percent, and now they are saying, can we lend a little bit more. There is no formal restriction, but in practice the market, the ratings, the triple A and all that, the World Bank formally cannot.

MS. BIRDSALL: Only the World Bank cannot.

MR. GURRIA: But then they have created private sector children. You have the IFC, but the IFC is $2.3 billion. The World Bank is $180 billion.

MS. BIRDSALL: We have to take you away.

MR. GURRIA: I know we have to go to American University but let me just make this point. One of the reasons is, how do you deal with the situation where the private sector is the one that now has to be doing these infrastructure projects, and the market is not yet prepared to lend long-term to the infrastructure projects done by the private sector. And you are financing dams and roads and infrastructure that need 20 years, 30 years, with five-year money?

The only 30-year money, the only 27-year money, the only 7-year grace period is provided by the international financial institutions, and they cannot, for practical reasons or legal reasons today, provide the same amount of money. So this consideration about whether the MDB should lend more to the private sector is critical. And just to answer your question, this is an issue that is of such relevance that it is one of the main issues in which the interim committee and the development committee and the G-7 and the G-10 are going to be focusing this week, and for the rest of the year, in fact.

There have been so many reports done by governments or by the institutions themselves, by the staffs, by the ministers, et cetera, and that's one of the reasons, again, why the relevance of the report is that it was done by independent people who did not belong either to the institutions or to governments.

MS. BIRDSALL: Any other questions?

Q -- Did the World Bank say they are going to [inaudible] low income countries?

MS. BIRDSALL: Did the World Bank say it?

Q   Yeah.

MS. BIRDSALL: The issue is that some shareholders at the World Bank, some groups in some shareholders, the World Bank is made up of member governments. So the decision in the long run, in the future, will be made by the member governments, and some of the member governments have more shares and more power in the institution than others. So this report is directed not to the bank itself, or to the management of the bank. It's directed to those who make decisions in the member governments about what they want their World Bank and their Asian Development Bank and so on to do.

MR. GURRIA: Actually, to be fair to the World Bank, they produced an internal stock report saying that they should continue lending to EMEs, and we are supporting that conclusion.

MS. BIRDSALL: Okay, thank you very much.