

# Restoring the Role of the World Bank and the RDBs

## *The Crisis and Beyond*

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# Overview

- Context
- Responding to the Financial Crisis
- Voice and Governance Reform
- Revitalizing the Role of MDBs in Development Financing

# Impact of the Financial Crisis on Emerging Markets and Developing Countries

- Impact deeper and more broad based than expected, with major downside uncertainties
- For emerging market economies (EMEs), main channels of impact are sharply decelerating export and private investment demand (with large negative multiplier effects) and loss of access to finance
- For low income countries (LICs), main channels of impact are falling export demand, deteriorating terms of trade, reduced remittances and declining private sector financing (including FDI)

# CHANNELS OF IMPACT

	ASIA	E. & C. EUROPE	LATIN AMERICA	SUB-SAHARAN AFRICA	MIDDLE EAST/ NORTH AFRICA
<b>FINANCIAL</b>					
Capital Flow Reversals	√	√√	√√		
Access to Finance	√√	√√√	√√	√√	√
Bank Distress		√√			
<b>ECONOMIC</b>					
Export Demand	√√√	√√	√√	√√	√
Commodity Prices			√	√√	√√
Remittances	√	√	√	√√	√
FDI	√	√√	√	√√	√
Investment Demand	√√√	√√	√		√

# Growth Impact Substantial with Major Downside Uncertainties

- EME and developing country growth expected to fall by 3 percent, with significant declines across all regions
- East Asia, Latin America, CIS and Eastern Europe most affected in terms of magnitude of slowdown
- Africa, Eastern and Central Europe and Latin America most vulnerable to downside uncertainties

# Employment and Development Impact Much Greater

- 20 million job losses in China—supply chain model suggests large spillovers in rest of East Asia from sharp export contractions
- Even relatively less open economies affected—1.5 million job losses in India in last 3 months
- Returning migrants and reduced prospects of overseas work adding to labor force pressures in many countries
- ILO estimates job losses of as much as 50 million as a result of the financial and economic crisis
- Large expected increase in poverty and impact on near-poor
- Setback on progress on MDGs especially in poorest countries

# Constrained Ability of EMEs and LICs to Respond

- Limited room for fiscal maneuver—constrained ability to undertake fiscal measures (financing rather than debt sustainability) and automatic stabilizers much smaller than in advanced countries
- Loss of access to financial markets, entailing in some cases large rollover risks
- Weak social safety nets
- Measures to assist developing countries will curb social and economic costs in the developing world as well as support global growth

# Magnitude of Financing Gap for Emerging Markets (\$ trillion)

## Financing Needs

• Current Account Deficit	\$1.2 - \$1.5
• Trade Finance	\$0.3 - \$0.4
• Rollover Risk	\$0.5 - \$1.5
• Capital Outflows	\$0.3 - \$0.8

## Financing Sources

• Private Capital (net)	\$0.3 - \$0.5
• IMF Actual	\$0.15 - \$0.25
• IMF Precautionary	\$0.1 - \$0.3
• World Bank	\$0.03 - \$0.035
• Other MDBs	\$0.05 - \$0.06

# MDB Response to the Financial Crisis

While the IMF is the focal point for the response to the systemic liquidity threat, the MDBs can play a critical complementary role in curtailing the spread and impact of the crisis:

- Financing for counter-cyclical fiscal measures targeted towards maintenance of jobs and protection of the poor
- Closing gaps and mitigating rollover risks in project financing including infrastructure, directly and by crowding in private and other official financing
- Catalyzing trade financing
- Supporting financial systems and credit flows to private sector and SMEs

# MDB Response to the Financial Crisis

Whereas a relatively small number of countries have so far made recourse to IMF programs, demand for MDB support is broad based amongst both EMEs and LICs. Meeting these demands effectively will require:

- *Speed* of response given the rapid downward spiral
- *Flexibility* to meet the needs of the broad but varying needs of emerging markets and developing countries
- Much larger *scale* of financing than anytime in the history of the MDBs

# MDB Response to the Financial Crisis

To meet this challenge, MDBs will need to:

- Put in place fast track mechanisms for agreement on and approval of emergency financing
- No conditionality or safeguards for budget support and use of established mechanisms
- Flexibility in application of operational and financial policy guidelines based on strong shareholder support
  - Lift ceilings for policy based lending
  - Flexibility in creditworthiness limits and portfolio guidelines
  - No change in pricing policies
- Assess adequacy of financing against scale of needs!

# IBRD Lending to Large Borrowers

Country	IBRD Outstanding Loans (million US dollars)	GDP (billion US dollars)	IBRD Outstanding Loans as % of GDP	IBRD Outstanding Loans as % of Total IBRD Portfolio
China	12,040	4,222	0.3	12.2
Brazil	9,892	1,665	0.6	10.0
Turkey	7,777	799	1.0	7.9
India	7,187	1,237	0.6	7.3
Indonesia	6,444	497	1.3	6.5
Argentina	5,263	339	1.6	5.3
Colombia	4,919	250	2.0	5.0
Mexico	4,117	1,143	0.4	4.2
Russian Federation	4,063	1,779	0.2	4.1
Philippines	2,690	172	1.6	2.7

<b>Total top 10</b>	<b>64,392.2</b>
<b>Total All</b>	<b>99,049.3</b>

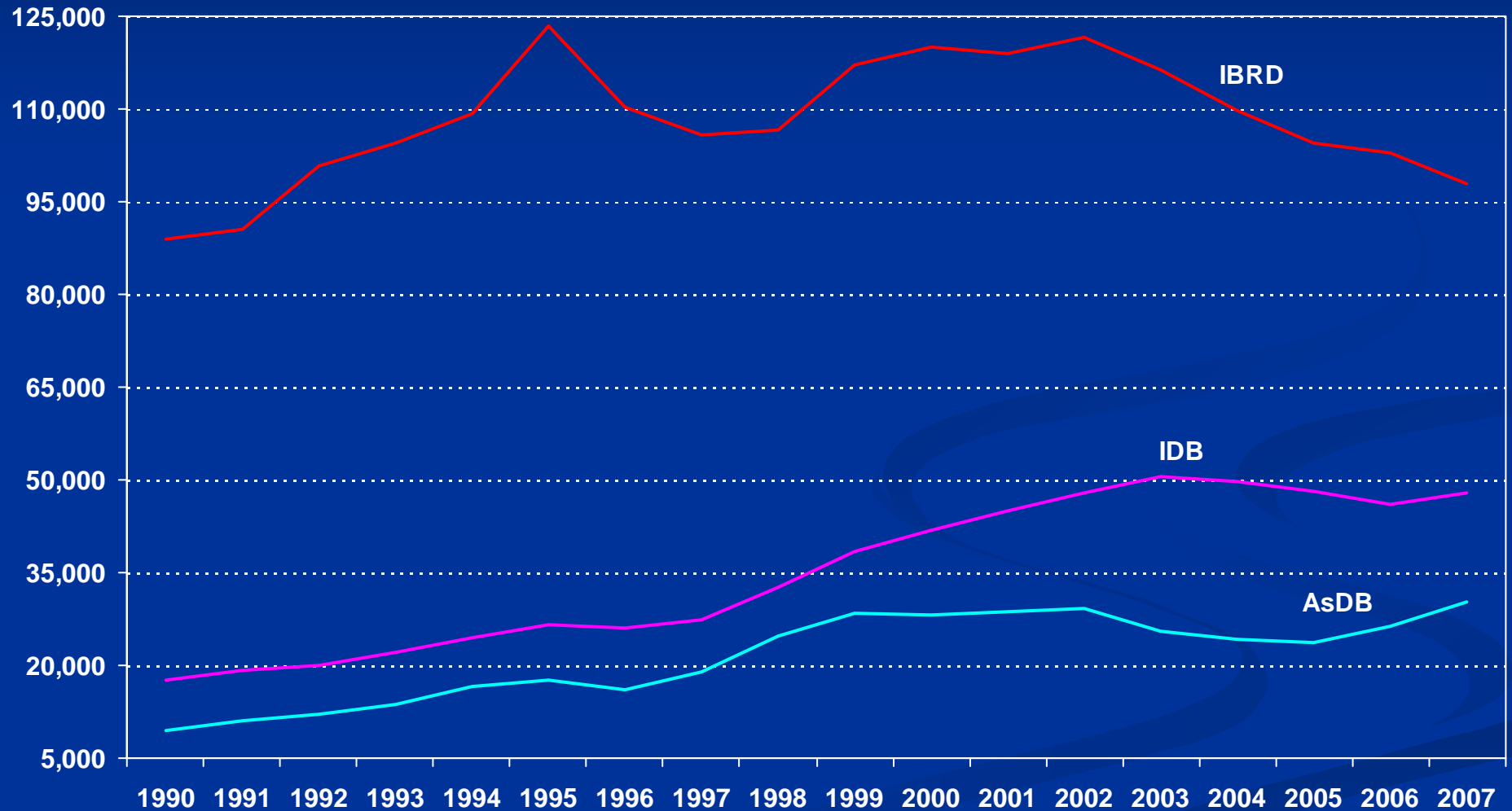
# MDB Response to the Financial Crisis

## Adequacy of Resources

- IBRD adequately capitalized to expand lending on the scale needed immediately
- Expedited capital increase for Asian Development Bank without new conditionality
- Bring forward reviews of capital adequacy for IADB AfDB and IFC
- Need to assess overall response capacity of IFIs
- Support front loading of IDA resources, but signal need for an exceptional mid-term review to augment IDA *without* additional transfers from IBRD/IFC
- Mobilize bilateral resources to augment MDB facilities for crisis response

# Outstanding Loan Portfolio of Multilateral Development Banks, 1990-2007

(US \$ Millions)



# Impact of and Response to Crisis in Low-Income Countries

	Baseline (US\$, billions)	Downside Scenario (US\$, billion)
<b>Financing Needs</b>		
Magnitude of Shock	165	324
BOP Gap	25	194
Additional Fiscal Needs	5-10	???
<b>Financing Available (2009-2010)</b>		
PRGF	3-4	
IDA	1.0	
AFDF	1.4	
Vulnerability Fund	4-5?	
Bilateral Aid	???	
SDR Allocation	Up to 15	

Source: IMF, G24 Secretariat

# Reform of Voice and Governance in the World Bank

- Initial package of reforms adopted at the last Annual Meetings (doubling of basic votes, partial offset for largest EMEs, and third chair for sub-Saharan Africa) was even more modest than the IMF with respect to voice and vote reform.
- IMF quota formula is not the right framework for World Bank reform (the best indicator is that the calculated quota for all of sub-Saharan Africa is 2.1 percent).
- A World Bank specific approach needs to be based on the development cooperative character of the institution, recognizing the role of those that it is intended to serve and those that contribute to its mission.
- Agreement and implementation of an ambitious second round should be brought forward to the Spring Meetings of 2010.
- Agreement must encompass and distinguish between IBRD, IDA and IFC.

# IMF Quota Shares and Voting Power Compared to the WB

	IMF			IMF		World Bank		
	Quota Shares Before Reform	Quota Shares After Reform	Calculated New Quota (New Formula)	Voting Shares Before Reform	Voting Shares After Reform	IBRD Shares	Total Votes	IDA Shares
Advanced Economies	61.6	60.5	64.4	60.6	57.9	58.7	57.4	57.7
US	17.4	17.7	19.0	17.0	16.7	16.8	16.4	12.5
Japan	6.2	6.6	8.0	6.1	6.2	8.1	7.9	9.8
EU-15	30.1	29.0	30.0	29.6	27.9	26.1	25.6	28.0
Other Advanced	7.9	7.2	7.4	7.8	7.1	7.7	7.6	7.3
Developing and Transition Countries	38.4	39.5	35.6	39.4	42.1	41.3	42.6	42.3
Asia	10.3	12.6	15.8	10.4	12.8	11.1	11.3	12.0
MENA	8.6	8.1	4.0	8.6	8.2	8.6	8.7	6.7
SSA	4.5	4.1	2.1	4.9	5.2	4.9	5.5	8.8
LAC	7.5	7.7	6.6	7.7	8.2	8.7	8.9	7.6
ECA	7.6	7.2	7.0	7.8	7.7	7.9	8.2	7.2
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
IBRD	73.4	75.6	83.9	72.3	72.7	74.8	73.4	56.6
IDA-only	11.8	10.3	5.7	13.1	13.7	12.9	14.4	30.2
Non-Borrowers	14.9	14.1	10.4	14.6	13.6	12.3	12.1	13.2
G11+Russia	33.4	34.1	30.9	33.9	35.5	35.6	36.2	32.4
Non-G11	66.6	65.9	69.1	66.1	64.5	64.4	63.8	67.6

# Impact of Additional Allocation of IBRD Shares

	World Bank		
	Total Votes	Total Votes Doubling	Total Votes (Doubling+ Unallocated Shares)
Advanced Economies	57.4	56.2	56.0
US	16.4	15.9	15.9
Japan	7.9	7.7	7.6
EU-15	25.6	25.1	25.0
Other Advanced	7.6	7.5	7.5
Developing and Transition Countries	42.6	43.8	44.0
Asia	11.3	11.4	11.5
MENA	8.7	8.7	8.8
SSA	5.5	6.1	6.1
LAC	8.9	9.2	9.2
ECA	8.2	8.4	8.4
Total	100.0	100.0	100.0
IBRD	73.4	72.2	72.2
IDA-only	14.4	15.8	15.7
Non-Borrowers	12.1	12.0	12.0
G11+Russia	36.2	36.8	37.1
Non-G11	63.8	63.2	62.9

# Objectives of World Bank Reform

- To make significant progress in adjusting voting rights and shareholding in light of members' evolved economic weight in the global economy and responsibilities for the development mandate of the Bank; and
- To strengthen Voice and Participation for countries whose weight in the World Economy may be small but for whom the Bank plays an important financing and advisory role
- Adjustment should not be at the expense of other developing countries

# Towards a World Bank Specific Formula

## I. Democratic Pillar

1. Basic Votes
2. Population

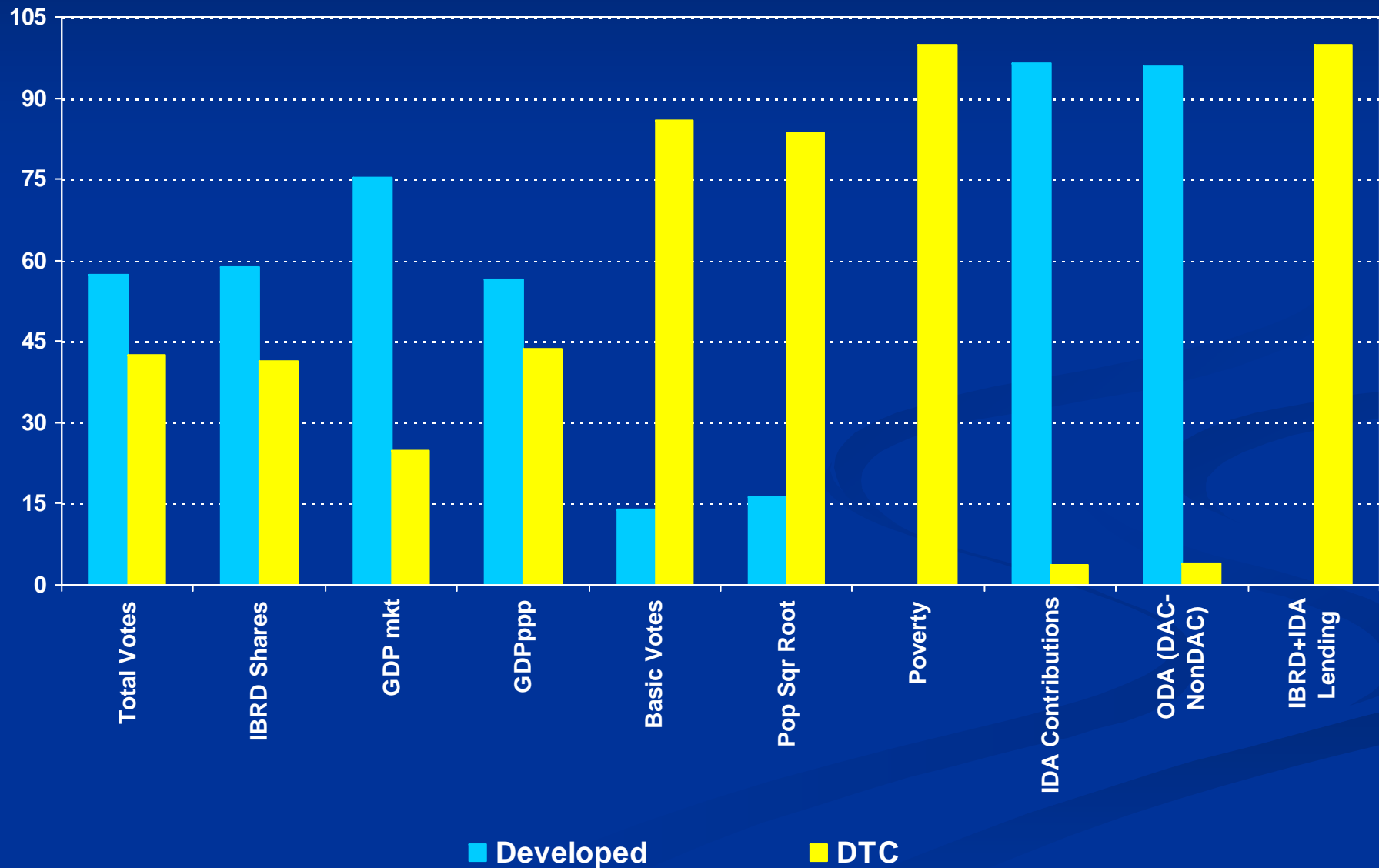
## II. Economic Pillar

1. GDP PPP

## III. Development Cooperative Pillar

1. Incidence of Poverty, IBRD/IDA Borrowing
2. IDA/ODA as well as indirect contributions

# Elements of a Possible Formula for World Bank Voting Structure



# Reform of Voice and Governance in the World Bank

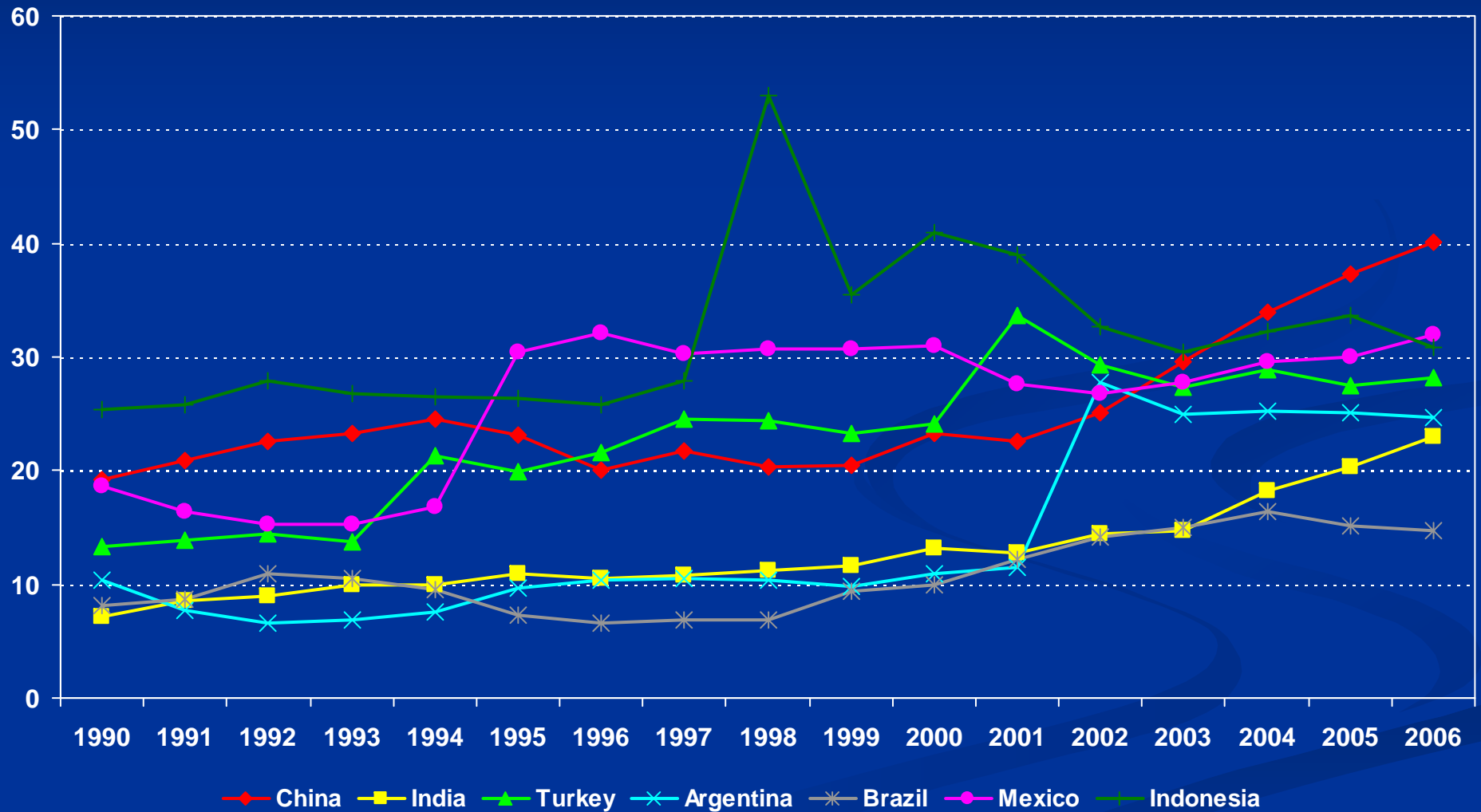
- In addition to voting reform, agreement to change the selection process for the Head and top management of the institution to an open merit-based process without regard to nationality, *beginning with the next appointments*, represents an early win in reform of voice and governance.
- Reform of composition of the Board and a review of decision rules should be pursued in the medium-term.
- A fundamental re-examination of the role of the Board and the Development Committee should be contingent on substantial progress on voice and vote reform.

# Revitalizing the Role of MDBs in Development Financing

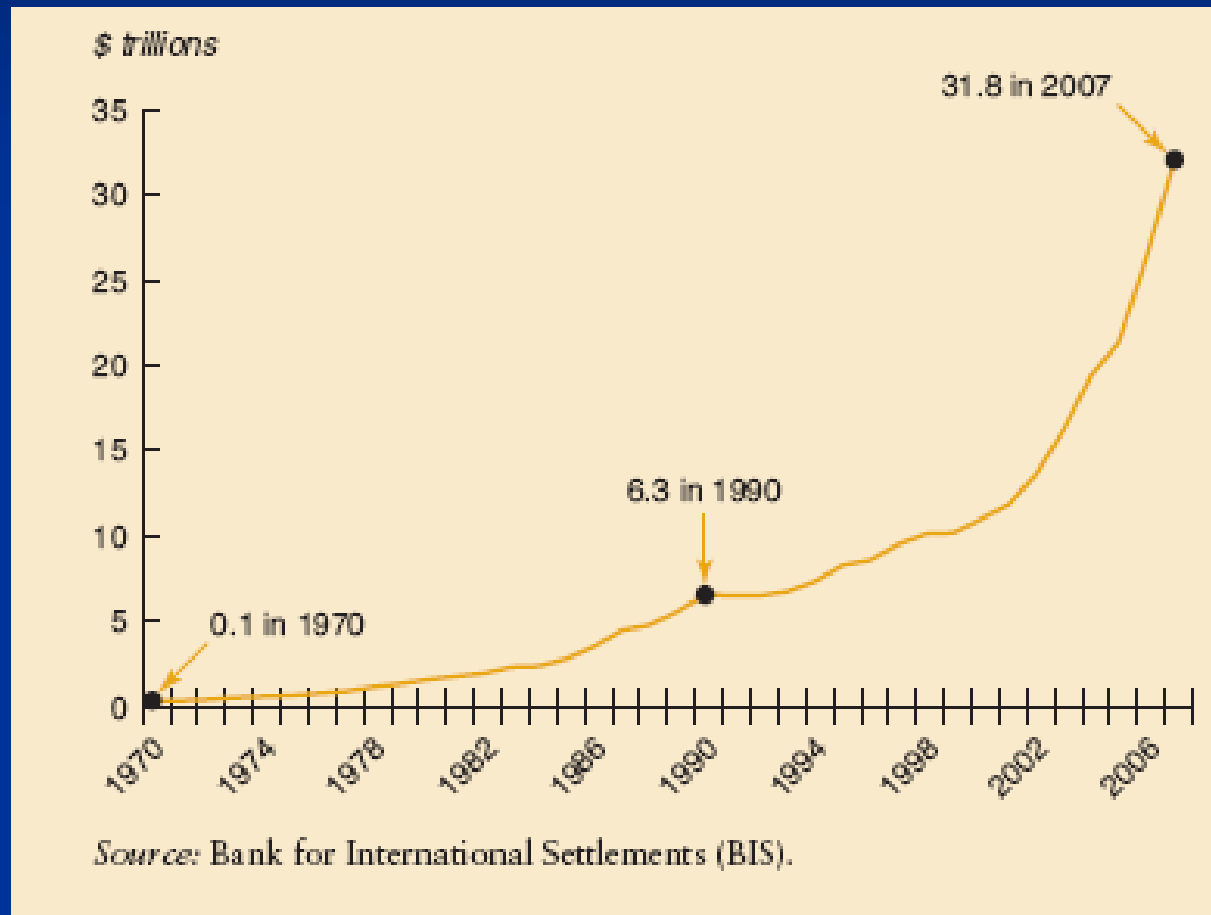
- Even after the crisis has abated, the global financial environment is likely to be much more difficult than the past eight years
- The wave of financial crises and cycles in private market flows have highlighted the high costs of borrowing from private markets for development financing (for countries that relied on market financing, typical costs of 20-50 percent of GDP since 1995)
- MDBs can play a critical role in mobilizing long-term market financing through its direct borrowing and by catalyzing stable private sector financing, and reducing risks arising from potential shocks
- MDBs remain the most effective channel to provide concessional financing for low income countries, and the combination of market financing and concessional arms provide a powerful means for augmenting and leveraging financing for maximum development impact across the range of EMEs and LICs
- MDBs have not been able to play this role because of a lack of a collective vision and will, lack of agreement on key operational policies and safeguards, and a governance structure that is skewed against those that have the greatest stake in the institutions.

# Exports of Goods and Services , 1990-2006

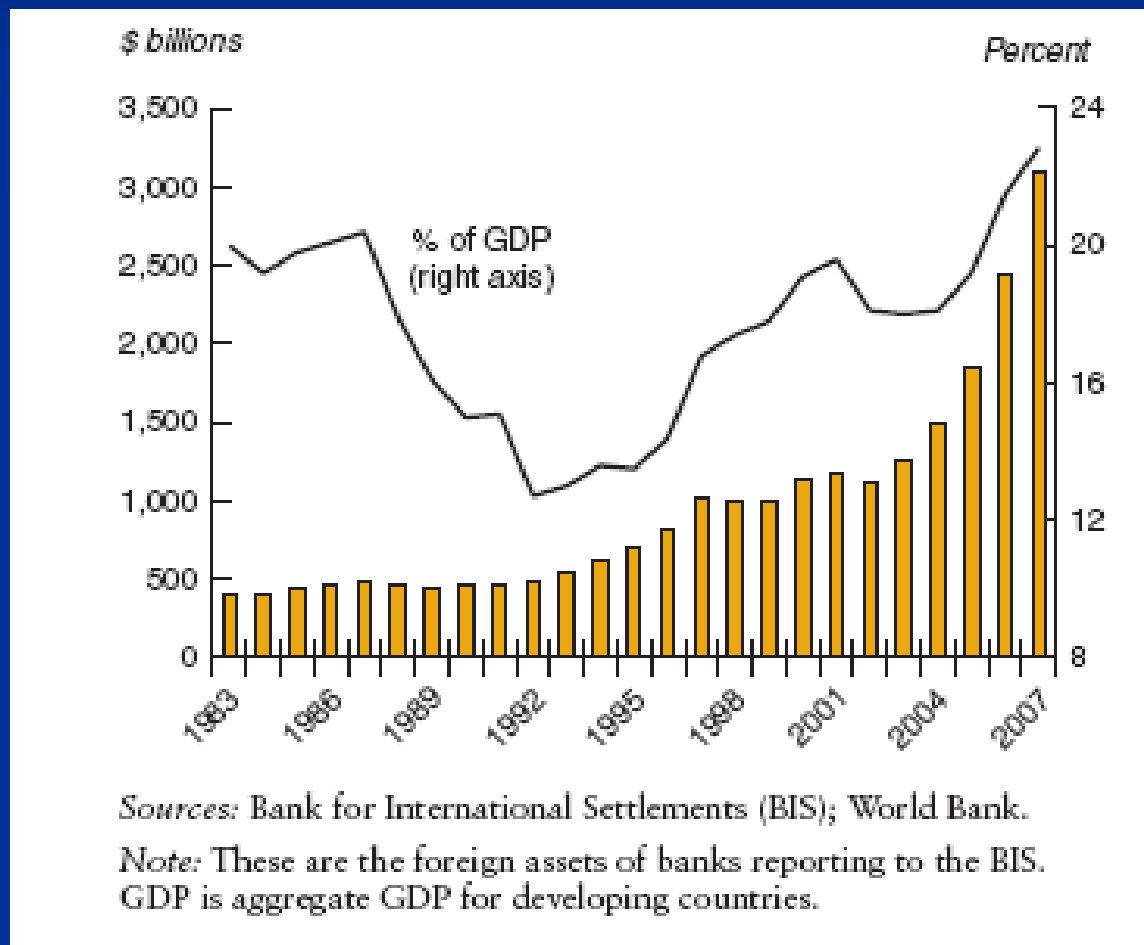
## (% of GDP)



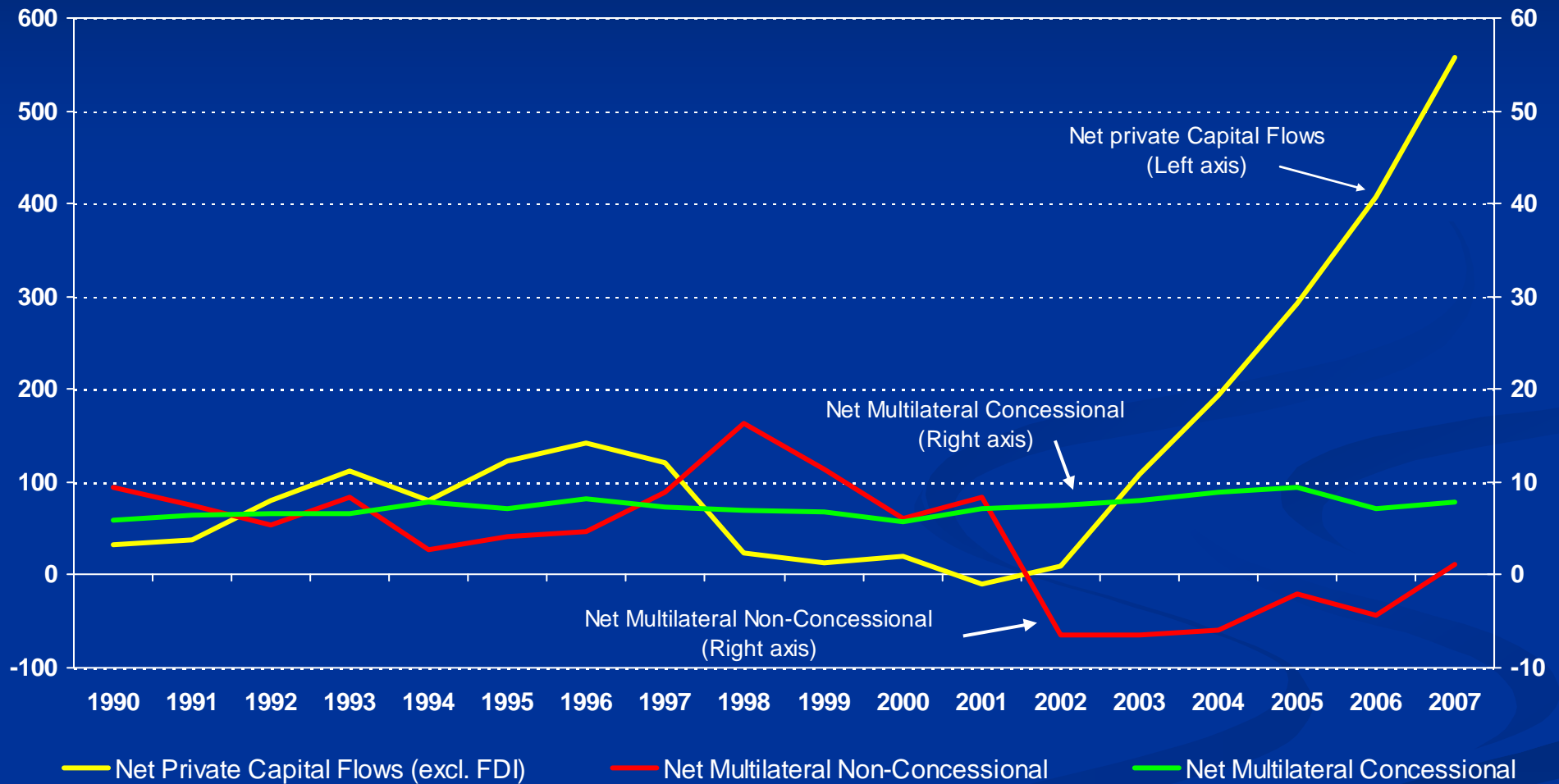
# International Banking Expansion, 1970-2007



# International Bank Claims on Developing Countries



# Net Private Capital Flows (excl. FDI) and Net Multilateral Lending, 1990-2007 (Billions, US\$)



# EMBI Spreads (bps)



# Revitalizing the Role of MDBs in Development Financing

Hence need for a clear and shared vision and strategy on the role of the MDBs:

- Learning lessons from the crisis, establish longer-term contingency financing arrangements including for “counter-cyclical” budget financing for countries with good track records
- More generally develop and aggressively deploy risk management instruments including flexible terms, GDP and commodity-linked bonds and local currency borrowing.
- Promote much greater use of guarantees to provide insurance and catalyze private financing.
- Drastically simplify lending requirements in line with the EIB model. Shift from an excessive focus on ex-ante safeguards and conditionality to country systems and ex-post evaluation.

# Revitalizing the Role of MDBs in Development Financing

- Grow the loan book to generate sustainable financing for concessional windows rather than mandate set levels of transfers.
- Introduce flexibility in debt sustainability frameworks and in mix of concessional and non-concessional financing.
- Move increasingly to output based measures to assess and allocate concessional aid.
- Commit necessary resources (capital, concessional funding) for MDBs to fulfill this mandate, including the ability to take on greater risk in their portfolios.