

MULTILATERAL DEVELOPMENT BANKS RAISING ECONOMIC GROWTH AND REDUCING POVERTY

INTRODUCTION - The MDB Growth Agenda

The United States is strongly committed to economic growth and development. In an era of profound global change, developing countries still face enormous challenges. The needs are clearly most acute for the poorest countries. The multilateral development banks (MDBs) continue to play an important role in assisting developing countries in their efforts to achieve greater economic growth and poverty reduction. The Treasury Department takes seriously its responsibility to do all that it can to ensure that the taxpayer resources provided to the MDBs make a more significant and sustainable improvement in the daily lives of the people living in developing countries.

The magnitude of the development challenge underscores the importance of the MDBs (and all other donors) according much greater attention to improving the effectiveness of their assistance. While we do not have all the answers to development, the international community can do a much better job in learning from our collective successes and our failures while thinking in innovative ways about basic problems. By measuring results you can see if a given activity is actually making a difference. And if it is not making a difference, then alternative approaches should be adopted. The United States is determined to continue to work with other shareholders to strengthen the effectiveness of the MDBs in this important endeavor.

We recognize and welcome the efforts that the MDBs have made to improve the development impact of their operations. However, we also believe there is a clear need for additional progress on a number of crucial operational and management issues.

Secretary O'Neill has called on the MDBs to increase their effectiveness in raising living standards around the world by focusing on projects that raise productivity. He has urged the MDBs to become more focussed, to improve their coordination with each other, and to promote productivity by placing greater emphasis on health, education and private sector development. He has urged them to promote aggressively the rule of law, enforceable contracts, property rights and a stable government process that can help to eliminate corruption. He has also called on the MDBs to increase the use of grants for funding activities such as health and education services in the poorest and least creditworthy countries.

In a good policy environment, external assistance can make an important difference. To maximize the development effectiveness of their resources, the MDBs should more substantially direct their resources to countries that demonstrate – not just commit to – sound policy actions.

Our agenda sets high expectations for the institutions as well as for the countries they serve. The MDBs must strive to do a better job at accounting for development results achieved, and for their individual roles in broader development efforts. As the MDBs reform, with the strong leadership

and support of the United States, they will remain essential contributors to the world's development efforts.

U.S. foreign assistance programs, including assistance through multilateral development banks, are important for advancing American foreign policy. The more our assistance aids in economic development, the greater countries' ability to engage in mutually beneficial trade with Americans, the greater the chances for democratic values to take root, and the greater the chances for government and social institutions to develop stability.

The crucial importance of laying the foundation for hope and opportunity have only been underscored by recent events. As the President has said, when governments fail to meet the most basic needs of their people, these failed states can become havens for terror.

OVERVIEW

Since its establishment in 1944, the World Bank's original mission of postwar reconstruction in Europe has shifted its focus to developing and transition economies. The World Bank, subsequently joined by four regional development banks, now seeks to encourage economic growth and poverty reduction, while specialized financial institutions like the Global Environment Facility (GEF) maintain narrower, specific mandates.

Today, the MDBs are essential instruments in achieving two of the most important international economic policy goals of the U.S.: raising economic growth and improving economic stability in the world economy. They also help serve important foreign policy goals, such as providing economic assistance to sustain key countries in the war on terrorism; combating money laundering and terrorist financing; providing assistance to countries emerging from conflict; and responding to natural disasters.

Over the past 25 years, the United States has consistently been the largest donor to the multilateral development banks. Our participation in the MDBs allows U.S. leadership and contributions to generate a greater volume of funds and a greater impact than available through unilateral action. In 2001, the U.S. provided \$1.2 billion in new funding, while the MDBs made commitments of \$45 billion. Historically, the MDBs have provided \$20 in development financing for every \$1 provided by the U.S.

While this additional financing generated by the U.S. contribution is significant, these institutions must significantly improve conditions for their principal constituency, the world's poor. As President Bush has said: "A world where some live in comfort and plenty, while half of the human race lives on less than \$2 a day is neither just, nor stable." Poverty today remains widespread and deep. Roughly 10 million children die needlessly each year, most from easily preventable diseases. More than 113 million primary school age children do not attend school, with forty percent of the children in Sub-Saharan Africa out of school. Over 1 billion people lack access to clean water and nearly 3 billion are without basic sanitation, leaving them vulnerable to disease. HIV/AIDS continues to spread relentlessly, leaving over 12 million orphans aged 14 or less in Africa alone, and is rapidly reversing the hard-won development achievements of many countries.

The magnitude and human consequences of the development challenge we now confront underscore the need for international development assistance efforts to do a much better job than they have been doing in increasing opportunities for people to create a decent living for themselves and their families. We can and must do better. The President's concerns about these institutions' performance have caused a significant change in the Administration's policies. As proposed by the President, the United States is working to negotiate a significant increase in the level of assistance provided to the poorest and least creditworthy countries as grants rather than loans. The United States and other donors are currently discussing replenishments for the International Development Association (IDA), the African Development Fund (AfDF), and the GEF. We are pursuing measures to increase the focus of these replenishments on countries with sound policy environments and demonstrated performance, and on operations that raise productivity. At the same time, the United States is emphasizing the need for all the MDBs to establish monitoring and evaluation systems with reliable performance and output indicators that measure development results.

Recognizing the importance of demonstrating results, the United States is also proposing a results-based financing framework for its contribution to the IDA replenishment. It provides a base-level annual contribution of \$850 million for each of the three years of the replenishment. Additional contributions of \$100 million in the second year and \$200 million in the third year will be made available if specific measurable results are achieved, for example, in the areas of education, health, and private sector development. This results-based concept is a new idea, put forth for the first time in the President's budget. It is one example of how we are emphasizing measurable results in our reform efforts.

Since foreign assistance can help only if the right fundamentals are in place -- including the rule of law, enforceable contracts, stable and transparent government, and a serious commitment to eliminate corruption -- we have worked hard with other shareholders in the MDBs to concentrate assistance on those countries with sound economic policies and good governance practices. For example, for the IDA-13 replenishment period, 17 countries will have their IDA lending allocations significantly reduced due to poor governance ratings. We have also worked to extend performance allocations to the soft loan windows of the African Development Bank and the Asian Development Bank.

We have also called for a greater focus by the MDBs on increasing job creating productivity growth. Rising productivity -- the amount of goods and services that each worker produces in a given amount of time -- has been the driving force behind increases in economic growth and rising per capita income and reduced poverty throughout history. An expanding, more productive economy, in turn, translates into better jobs, increased wages, and a higher standard of living for all. An advantage of the focus on productivity is that we already know a great deal about what enables people to become more productive. These include building human capital and foundation institutions such as legal systems, offering the right incentives to reward hard work, removing government-generated obstacles to business, teaching new skills, and even developing things that many of us take for granted, such as functioning sewer systems and clean water to stave off disease. Therefore, by looking at productivity, we are focusing attention on those areas that really make a difference to people's standard of living.

As a result of U.S. efforts, productivity and private sector job creation are receiving more emphasis in the debate on MDB policies within the institutions and among other shareholders. We will continue working actively to ensure it becomes a hallmark of actual operations. We are aggressively pursuing this MDB growth agenda. If we stay the course, we can make a very meaningful difference in the lives of millions of people by helping them to realize their potential as productive, thriving citizens of the world.

The Administration's FY 2003 budget request for the MDBs includes \$1,259.4 million to fully fund annual U.S. commitments, and \$177.7 million as part of a 3-year plan to clear U.S. arrears to the MDBs which now total \$533 million. This funding will help enable the MDBs to address critical development issues in key regions, project U.S. leadership, and further our reform efforts to strengthen the effectiveness of these institutions.

The remainder of this paper is divided into three sections. The first two sections provide examples of how the MDBs have helped advance U.S. economic and foreign policy goals. These sections are similar to what has been provided in previous years' reports, although they focus on key U.S. priorities such as promoting productivity and combating terrorism. The third section lays out in greater detail the U.S. MDB growth agenda just described and provides an update on recent achievements. More detailed information on the operations and policies each MDB can be found in separate tabs toward the end of this report.

A. PROMOTING ECONOMIC GROWTH, INCREASING PRODUCTIVITY GAINS AND RAISING LIVING STANDARDS

The MDBs are placing greater emphasis on improving productivity, and thereby increasing economic growth and reducing poverty. These include (1) improving education and health; (2) promoting private enterprise, including small and medium enterprises; (3) promoting rule of law, enforceable contracts and property rights, effective public expenditure management, accountability and anti-corruption efforts; (4) opening economies and strengthening trade capacities and investment environments; and (5) supporting sound environmental and labor policies in countries around the world.

1. Building Capacity through Investments in Human Capital and Health Care

People need good health, knowledge and skills if they are to become more productive. Yet, too many people in developing countries lack basic education and health care. The scourge of AIDS and other infectious diseases is inflicting an enormous toll on populations in Asia, Latin America and, especially, Sub-Saharan Africa. The MDBs have played an active role in supporting health and education systems in developing countries:

- **The World Bank is the world's largest external funder of health programs and of efforts to combat HIV/AIDS. The Bank has committed \$2.3 billion to combat the spread of HIV/AIDS and has pledged that no country with an effective HIV/AIDS-fighting strategy will go without funding. The Bank has also been asked to take on the trustee function for the Global Fund to Combat AIDS, TB and Malaria.**
- The World Bank is also the world's largest external funder of education, with 164 projects under implementation in 82 countries, representing some \$11 billion in commitments. It has supported efforts in India to enroll an additional 10 million children in schools over a five-year period, and helped Guinea increase the enrollment of girls in primary schools by 12 percent over the past 11 years. Lending for education is expected to be about \$1.5 billion annually starting in FY2002, with continued growth expected for the next few years.
- The AsDB has committed to increase basic health lending by over 50 percent over the next fiscal year to nearly \$340 million. Last year, it provided grants to Cambodia, Laos and Vietnam to help combat HIV/AIDS, and funded projects in Pakistan, Indonesia, Bangladesh, Cambodia and Vietnam to strengthen immunization programs and train health workers.
- The AsDB expects to increase its lending for education to 8.5 percent of its portfolio in 2004, up from 6.5 percent currently, with the bulk of it going to countries with the lowest education rates and greatest need. Basic education projects in Bangladesh and Pakistan are keeping girls in school. An education project in Laos is providing support to 300 ethnic minority villages that have traditionally lacked access to education.
- The IDB is at the forefront of efforts to increase access to, and improve the quality of, education provided in Latin America and the Caribbean. In 2001, the IDB financed \$711 million in education projects.
- The AfDB has committed \$351 million to the health sector since 1990, with a growing share (20 percent in 2001) going toward HIV/AIDS control. It is also helping to improve education in Africa. One project helped double the total number of students in school in Cape Verde, while another in Kenya reduced infant mortality by 30 percent in the project area.

2. Encouraging Private Enterprise and Market-Oriented Mechanisms

Private capital flows now dwarf official development assistance. The challenge is to deploy development assistance in areas where we know it will unleash the entrepreneurial and creative capacities of people living in the poorest countries. The MDBs have helped shift countries' policies away from excessive state-control and towards market-oriented systems around the world. All of the MDBs are focused on the development of sound regulatory, supervisory and legal frameworks for the private sector in developing countries. All MDBs have played a role in supporting small and micro enterprises throughout the world -- a role we want to expand. We believe the MDBs can do a better job in integrating policy reform, technical assistance and private investment, and in prioritizing investment climate reform as a core element of their lending operations and policy dialogue.

- The MDBs have supported privatization in the banking, telecommunications, railroad, coal, water and agricultural sectors around the world. For example, the World Bank helped Pakistan privatize state-owned banks, as mandated by their IMF program, and facilitated Colombia's incorporation of the private sector into the management and operation of water utilities. The EBRD supported the privatization of Estonia's railway company, Hungary's national telephone company (now publicly traded), and the Croatian pharmaceutical firm Pilva (also now publicly traded). The AfDB supported the privatization of Tunisia's post and telecommunication sector, while the AsDB assisted the Kyrgyz Republic in privatizing state-owned enterprises, with an emphasis on corporate governance.
- The World Bank and the EBRD supported the successful reform of Russia's inefficient and politically sensitive coal sector, extended credit to a large number of small and medium-sized enterprises and supported the modernization of Russia's tax system.
- The IFC arranged \$3.9 billion in committed funding for private companies in 2001 and is seeking greater involvement in high-risk "frontier" markets, such as sub-Saharan Africa and Central Asia. Its E-Finance Initiative is developing and disseminating new technologies and practices to encourage local bank lending to small and medium enterprises.
- Last year, the EBRD committed \$3 billion in financing to the private sector. It disbursed 12,000 small and medium-sized loans amounting to \$550 million, and continued to administer U.S. funds provided under the Support for Eastern European Democracies Act to promote small and medium sized enterprises.
- MDB investments in agriculture help generate productivity in areas where 75% of the world's poorest people live. For example, in Guinea, an AfDB project trained 450 farmers in new farming techniques, thereby increasing crop yields and providing more than 1500 permanent jobs and thousands of seasonal jobs. The International Fund for Agricultural Development (IFAD) devotes its entire annual lending program of about \$450 million to programs designed to alleviate rural poverty.

3. Good Governance and Anticorruption Measures

The MDBs have been active in providing assistance to countries to combat corruption. The World Bank alone has introduced 600 anticorruption programs and good governance initiatives in almost 100 countries since 1996. The MDBs also fund a large number of analytic and advisory activities to help diagnose governance problems, and are also strengthening their internal controls to ensure that funds go to their intended use. At U.S. urging, governance and corruption are routinely discussed in MDB country strategies, and more assistance is being provided to help countries tackle corruption issues. Outcomes of such assistance include:

- the introduction of public expenditure tracking surveys that reformers in Uganda have used with success to help ensure that expenditures are spent on their intended purpose;
- improved government procurement procedures in Nicaragua, Honduras and Paraguay;

- stronger judiciary systems in Venezuela, Nicaragua, Jamaica, the Dominican Republic, Uruguay and Bolivia;
- civil service reforms in Bolivia and a merit-based system of selection of judges in Georgia, which resulted in the replacement of 80% of judges sitting in the first round of examinations;
- support for Indonesia's creation of an independent anti-corruption agency, public procurement reforms, and judicial reforms;
- reform of public procurement systems in Tanzania, Benin, Chad, Cameroon and Sierra Leone; and
- training of investigative journalists to cover corruption issues in their countries.

The MDBs have also strengthened their internal controls to guard against possible corruption. All have investigative units or mechanisms as well as staff codes of conduct that prohibit unethical or fraudulent practices. Most have established hotlines for reporting allegations and protections for whistleblowers. And they have made progress on harmonizing procurement documents across MDBs.

4. Opening Economies to Trade and Investment

Trade liberalization is essential to economic development. Research shows that trade has been a major driver of economic growth for the last three decades. Since 1980, per capita incomes of developing countries that have lowered tariffs and increased actual trade volumes are closing the gap with richer countries, while "non globalizers" are falling further and further behind. Trade liberalization promises large long-term benefits to the United States and other countries, and the MDBs have an important role to play in encouraging countries to reduce trade and investment barriers:

- The World Bank has increased its efforts to assist countries improve their capacity for trade and to integrate trade issues into Bank programs. It has taken a lead role in revamping the Integrated Framework, a mechanism for coordinating and providing trade-related assistance to the least-developed countries, and plans further work in response to the November 2001 Declaration of the Fourth WTO Ministerial Conference in Doha, Qatar. Its new private sector strategy proposes the drafting of investment climate surveys for all borrowers.
- EBRD supports trade and investment liberalization as a core part of its mandate. For example, EBRD has supported the removal of financial constraints to trade through its trade facilitation program. It has also financed infrastructure projects to remove the physical constraints to trade. For example, the EBRD is providing \$53 million to Romania to reform its road sector and enable the construction of a main road to the west of Romania, which will help facilitate intra-European commerce. It also promotes investment liberalization through policy dialogues with governments on issues such as regulatory reforms and through projects that increase foreign direct investment (FDI).

- AsDB is providing assistance to Indonesia to promote deregulation and provide a level playing field for all businesses, including small and medium enterprises. It is helping the government simplify the regulatory framework; remove barriers to domestic competition and trade; and strengthen the policy framework governing domestic investment and FDI.
- AfDF-9 negotiations are expected to include an increased focus on regional economic cooperation and integration in Africa, including through better diagnostics and increased staff. The Fund will also undertake limited and targeted policy-based loans aimed at promoting regional integration.
- The IDB is supporting efforts to negotiate a Free Trade Area of the Americas (FTAA) through comprehensive technical and logistical support through the Tripartite Committee and ongoing support for more than 20 hemispheric cooperation programs. Also, the MIF is providing technical support for implementation of eight trade promotion measures for customs procedures.
- The IFC is increasing its activities in Jordan by helping to finance infrastructure investments and businesses that will benefit from the new U.S./Jordan Free Trade Agreement.
- IDA is helping Albania foster trade by promoting more efficient and less costly trade flows and providing European Union-compatible custom standards.

5. Financial Crisis Prevention and Response

Recently, we have seen that the financial markets are differentiating more among emerging market economies, reducing the potential for far-reaching contagion of financial crises. This is an important development. However, it is essential to prevent the eruption of financial crises in the first place. Here, the MDBs are increasingly providing assistance to improve the structure and transparency of financial systems, the profile of public debt and the effectiveness of social safety nets in order to make economies more resistant and resilient to shocks.

MDB financing can only be effective when the borrowing country puts in place the right policies. IFI financing alone is not able to overcome a poor macroeconomic policy environment. Tough decisions need to be made concerning when to withhold financing until credible plans are proposed by a government that can lead to a path of sustainable growth. Once credible reform plans are being implemented, in coordination with the IMF, the MDBs can provide complementary resources that have a much greater chance of achieving real long-term results.

The MDBs are also playing a key role in accelerating the emergence of transparent and well-regulated financial sectors. In close coordination with the IMF, MDB operations are helping reform and modernize financial sectors by facilitating strengthened surveillance and preventative measures, as well as by promoting core policy reforms.

- The World Bank and the IMF are working closely together on the joint high-level Financial Sector Liaison Committee (FSLC) to coordinate efforts to promote financial sector reform. They worked closely together, with international regulatory bodies and with the Financial

Stability Forum, to develop and refine financial sector standards and assessment methodologies to assess how members implement best practices.

- Under the joint World Bank-IMF Financial Sector Assessment Program (FSAP), 21 countries have been reviewed and have received expert advice on strengthening their financial sectors. The Bank and the Fund anticipate assessing 24-30 countries per year, and are intensifying their technical assistance to follow up on the recommendations coming out of these assessments.
- World Bank country strategies, which are key planning documents for future lending, when appropriate, include issues emanating from the FSAPs. These documents identify priority policy reforms and specific restructuring needs, and Bank efforts to address them.
- The Inter-American Development Bank (IDB) is helping to strengthen social safety nets and support financial reforms, including through greater access by small and medium-size enterprises to credit. The Multilateral Investment Fund (MIF) is funding training in supervision and regulation, including ways to combat financial crimes.
- AsDB is working to increase corporate and banking sector transparency, strengthen capital market regulation, and raise standards of business governance and financial disclosure.
- The EBRD's work on financial sector reform is helping prepare countries to respond to financial crises, and well as prevent them.

6. Supporting the Environment

The MDBs have adopted policies and procedures to incorporate environmental considerations into their analyses and operations. Environmental assessment and mitigation plans are routine, and the banks have strengthened compliance procedures to help ensure work is done right. Inspection panels have been created to provide a public forum to resolve problems. Environmental components such as energy efficiency improvements are now often incorporated into projects and sectoral programs. Technical assistance and training have helped build environmental management capacity in many countries. Support for sustainable development has steadily increased in nearly all the banks. Recent developments include:

- From 1990-2000, the World Bank lent about \$7 billion for stand-alone environmental projects and another \$11 billion for environmental components of sector projects. It recently established a new environment strategy, revised its resettlement policy and is trying to improve the impact of interventions in the environmental health area. IDA donors have adopted several environmental principles in its 13th replenishment, including consideration of the environmental implications of adjustment lending.
- The third GEF Replenishment negotiations include plans to expand GEF operations to finance projects that address persistent organic pollutants, which directly affect a number of U.S. states.

- The AfDB adopted a policy for integrated water resources management, environmental assessment procedures for private sector operations, and is revising its environmental policy.
- The AsDB is developing a new environment policy and is seeking opportunities to simultaneously improve productivity and protect the environment. For example, it developed an acid rain control project based on improving the efficiency of industrial processes in highly polluted cities in China.
- The IDB adopted a new energy sector strategy that aims to help develop more efficient and sustainable patterns of energy production and use.

7. Promoting Internationally Recognized Labor Standards

The MDBs now review core labor standards in country assistance strategies and are committed to ensuring that their projects do not violate internationally recognized labor standards, and are being proactive in trying to address child labor and forced labor in borrowing countries. There is also better consultation with workers in project preparation and implementation, and greater emphasis in MDB operations on worker safety issues.

- In 2001, the World Bank Group intensified its efforts on child labor, with specific attention to vulnerable groups of children, including HIV/AIDS orphans. The IFC is building on its 1998 Policy Statement on Forced and Harmful Child Labor by developing "good practices" that it can share with borrowers and to help them combat child labor issues among their suppliers.
- Last year, the MIF continued to provide critical support for upgrading labor skills and working conditions, and the IDB approved a project to enhance labor markets in Mexico and a project, among other things, to fight child labor in Brazil.
- The EBRD has included labor issues in country strategies since 1999. We have worked to ensure consistent treatment of relevant labor issues in the strategies and in investment operations. Most countries in the region have laws that provide labor protections, and the EBRD requires borrowers to comply with all national laws, including labor laws.
- The AfDF has developed a strategy for dealing with labor standards and is developing a checklist of guidelines on these issues to be used in policy discussions on country strategy papers (CSPs). Since 1999, all new CSPs feature a section on labor standards.
- The AsDB recently adopted a safeguard policy that requires compliance with core labor standards in AsDB loans. It is also providing support to reduce child labor and bonded labor and to promote core labor standards in a number of countries.

B. ADVANCING U.S. FOREIGN POLICY OBJECTIVES

The MDBs help to support economic growth and reform in key regions and countries that are joining in the fight against terrorism and money laundering. They also provide support to post-conflict countries and respond to natural disasters.

1. Economic Support for Regions and Countries

Afghanistan: The World Bank and the Asian Development Bank, together with the UNDP, are coordinating the international effort to respond to Afghanistan's urgent reconstruction needs. They helped organize a recent international donors' conference that resulted in aid commitments of \$4.5 billion. The World Bank has indicated that it is prepared to provide \$500 million in assistance to Afghanistan over the next 2-1/2 years, and \$50-70 million in immediate grant assistance. Over this period, the AsDB is considering providing \$500 million in assistance, including grants.

Turkey: Over \$1 billion was provided to Turkey by the World Bank in 2001 to support urgent reforms in the public sector and banking system, to reduce agricultural subsidies, and to strengthen Turkey's social safety net. The IFC provided long-term financing to private manufacturers who have been unable to access commercial financing because of national economic problems.

Pakistan: The World Bank and the AsDB have provided substantial support for economic development in Pakistan. As Pakistan's economic performance improves, the MDBs are prepared to extend \$3.3 billion over 3 years to support programs and reforms in health, education (especially for women), good governance, financial market development, basic infrastructure and the power sector.

Central Asian Republics: The World Bank, the AsDB and the EBRD have all enhanced their work with the Central Asian Republics to help them make the transition from centrally planned economies to market economies, strengthen their governance procedures, and promote intra-regional trade and investment in order to reduce the risks of instability.

Philippines: The World Bank is helping the Philippines improve its water supply and urban transportation system, strengthen its financial sector and improve governance, all of which are vital to the Philippines' effort to fight poverty and help provide the wherewithal to combat terrorism. The AsDB is focusing its efforts on Mindanao, where most of the poor live.

Indonesia: The World Bank provided over \$490 million to Indonesia in WB FY 2001 to strengthen social services and improve the environment.

Sub-Saharan Africa: The World Bank and the AfDB are helping African nations to combat the scourge of HIV/AIDS. The enhanced HIPC initiative is expected to channel an additional \$1 billion annually into social sector spending under policy reform, helping to alleviate poverty in the poorest countries of the world.

Colombia: Last year (CY 2001), the World Bank and the IDB provided nearly \$1 billion to Colombia in support of social services and financial management. This support will make it easier for the Colombian Government to stem the tide of illegal drugs.

2. Combating Terrorist Financing

Global terrorism is a serious threat to the very foundation of our economy and society. The MDBs are an active, strong partner in the global effort to combat money-laundering and terrorist financing. They have provided technical assistance to help establish financial intelligence units and/or strengthen money-laundering regimes in countries around the world, including Indonesia, Albania, Russia, Turkey, Ukraine, Colombia, Guatemala, Jamaica and Nicaragua. They are also improving their analysis of country procurement systems and financial sectors to help governments better understand their vulnerability to financial abuse so that they can target their efforts more effectively.

The World Bank is working with the IMF to include in financial diagnostic tests an assessment of vulnerability to money-laundering and terrorist financing. They are also enhancing their analysis of Middle Eastern banking systems and improving their understanding of alternative payment systems, such as “hawala”, which are commonly used by terrorists.

The MDBs have also taken steps to strengthen their due diligence procedures for monitoring their own and borrower use of funds to prevent any MDB funds from inadvertently going to support terrorism.

Finally, the MDBs are helping to combat terrorism in other ways, including by helping to support effective judicial systems, honest custom services, and improved airport security -- all of which are essential to this effort. For example, the MIF created a \$10 million grant program to help strengthen airport security in Latin America and the Caribbean.

3. Providing Post-Conflict Assistance to Keep the Peace

Increasingly, poverty appears to be both a cause and a consequence of conflict. Therefore, the MDBs have provided post-conflict reconstruction assistance in nearly 40 war-torn countries to help keep the peace and reduce poverty. These include programs in Afghanistan, the Balkans, the Democratic Republic of Congo, Cambodia, East Timor and other countries. For example:

- The World Bank has provided nearly \$600 million to Ethiopia and Eritrea for post-conflict recovery since June 2000, including funds to demobilize and integrate veterans, rehabilitate infrastructure, facilitate the return of displaced persons, and combat the spread of HIV/AIDS.
- The World Bank and IDA provided \$240 million to the Balkans for basic infrastructure and services in 2001, and contributed \$35 million to an international trust fund.
- In 1999, the World Bank provided \$75 million for post-conflict recovery and reconciliation in Sri Lanka, including efforts to rehabilitate irrigation and other infrastructure. The AsDB is providing support to Sri Lanka to help with rehabilitation and conflict prevention.

- In July 2001, IDA approved a \$50 million post-conflict grant for the Democratic Republic of Congo to provide technical assistance for economic reforms, capacity building, and aid coordination.

4. Responding to Natural Disasters

In the wake of natural disasters, the MDBs have provided finance to respond to humanitarian needs and rebuilding efforts, and have increased attention to disaster prevention. Following two earthquakes in El Salvador, the IBRD agreed in 2001 to provide up to \$270 million to El Salvador over the next 3 years, including a \$143 million project for reconstruction and health services extension, while the IDB provided \$40 million for earthquake relief. After earthquakes struck the Gujarat State in India, the World Bank and AsDB approved \$900 million in early 2001 to meet immediate housing and infrastructure needs and to finance longer-term recovery efforts.

When Mozambique suffered a devastating cyclone and flooding in early 2000, IDA and the AfDB provided more than \$30 million for disaster recovery efforts. This enabled Mozambique to maintain macroeconomic stability while rebuilding vital infrastructure. Similarly, following earthquakes in Turkey in 1999, the World Bank provided more than \$1 billion to finance reconstruction, private sector imports and development of a disaster response system.

Following the devastation of Hurricane Mitch in 1998, the IDB provided in 1999 a regional grant to help Central American countries strengthen their efforts to prevent and mitigate the effects of natural disasters. The World Bank responded with a three-pronged strategy that involved assistance for short-and medium-term rehabilitation; emergency financing, macroeconomic assistance and debt relief; and longer-term reconstruction.

The MDBs are also financing operations to strengthen countries' own capacity to deal with natural disasters. For example, a \$400 million World Bank loan to Mexico in 2001 supports wide-ranging initiatives to reduce vulnerability to natural disasters and to support rapid recovery when disasters do occur. The Bank is also helping Grenada and Nicaragua strengthen their preparedness for natural disasters, and Belize to improve water drainage to handle floods.

C. U.S LEADERSHIP FOR INSTITUTIONAL CHANGE

Reform of the multilateral development banks is one of the highest priorities of the U.S. international economic policy agenda. Our reform effort has two broad themes. The first is to call for greater MDB focus on increasing productivity growth. Higher productivity means higher incomes, higher standards of living, and lower poverty. Focusing on productivity also provides a way for the MDBs to set priorities. The U.S. is aggressively promoting this focus by insisting that every project, every program, every loan and every grant be judged by the standard of how much it will increase productivity.

The second broad theme is emphasizing measurable results -- that is, looking at the activities that are undertaken by the institution and seeing exactly where they make a difference, how much of a difference, and compared to what other activity. This means insisting on more rigorous

quantifiable measures of the impact of each aid project and on accountability for each institution's impact on improving living standards; further strengthening performance-based allocations; improving coordination among MDBs in order to reduce unnecessary overlap; reforming and making more transparent MDB budget procedures; and further increasing disclosure of documents.

It also means that each MDB should focus on its area of comparative advantage rather than attempt to be a supermarket of development lending. These institutions are not fundamentally competing with each other. Rather, they are parts of a system.

Increased Grants: The U.S. has called upon the development banks to increase the amount of assistance they provide in the form of grants, rather than loans. Specifically, President Bush has proposed that MDBs provide up to 50 percent of their assistance to the poorest and least creditworthy countries in the form of performance-based grants. The goal of this proposal is to break the cycle whereby the poorest countries pile up unsustainable debt burdens. In recent years, much of this debt has been forgiven because debt repayment would have entailed diversion of funds from priority development activities such as education, health and rural development. Development programs would be better served by transparent grant funding, and grants should be closely tied to performance.

Measuring and Evaluating Results: The MDBs have taken steps to improve their ability to measure progress and outcomes. Most have put in place more rigorous monitoring of project implementation with assessments of project performance, including the share of projects that are at risk and need careful monitoring and/or corrective measures. Additional efforts to improve the focus on monitoring, evaluation, and measurable results are essential. It is currently very difficult to attribute credit for success among borrowers, the MDBs, and other donors. The concept of "success" of an MDB project needs to be measured more in terms of the actual impact the project has on the people it is intended to help. It is important to move MDB evaluation work (both lending and technical assistance) toward assessment of the output/impact on living standards in borrowing countries, in addition to existing audit and process evaluation. It is also important to assess how effective MDB operations are in leveraging the other primary sources of development resources (e.g., private domestic savings, FDI, trade).

As part of a broader international effort to leverage aid to achieve poverty reduction results, all of the MDBs have committed to working towards the goals of the U.N. Millennium Declaration approved by Heads of State in September 2000, including:

- Reduce the proportion of people living in extreme poverty (less than \$1 per day) by half between 1990 and 2015.
- Enroll all children in primary school by 2015, and remove discrimination against girls in primary and secondary education by 2005.
- Reduce child mortality by two-thirds between 1990 and 2015.
- Reduce maternal mortality by three-quarters, between 1990 and 2015.
- Halt the spread of HIV/AIDS, malaria and other major diseases by 2015.
- Halve by 2015 the proportion of people without sustainable access to safe drinking water.

Furthermore, in addition to strong U.S. advocacy for the MDBs to more routinely, systematically and publicly measure and report on progress towards a set of priority growth and poverty reduction goals, IDA has proposed to institute a monitoring system to track progress towards a small, but high-development impact set of performance triggers in the areas of education, health and private sector development. The U.S. continues to urge other IDA donors to join us in conditioning additional contributions to achievement of these goals.

Performance-Based Allocations: Research clearly shows that assistance is more effective when it is provided to countries that are committed to and successful in implementing sound economic policies. It also shows that in a good policy environment, assistance attracts investment because it increases private sector confidence and helps to provide public services (e.g., education and infrastructure) that investors need. On the other hand, research shows that providing assistance to countries that are not committed to good policies can actually be counterproductive, particularly when provided in the form of loans which add to countries' debt burdens. The World Bank, the AfDB and the AsDB are now allocating concessional resources on the basis of country performance. Each MDB has a process for assessing performance based on measures of various indicators, with a strong emphasis on country performance on good governance. For the IDA-13 period, 17 countries will have their IDA lending allocations significantly reduced due to poor governance ratings.

Performance-based contributions: The U.S. has advanced a proposal for a results-based contribution to IDA-13 that provides an incentive for additional funding contingent both on explicit inputs necessary to design relevant and more successful assistance programs, as well as measurable development outcomes in select areas crucial to growth and poverty reduction. We are developing timelines and indicators that would provide credible triggers for the incentive contributions. Since the evaluation period to determine the first incentive contribution is short (roughly one year), the first set of triggers will be **input-based**. The second incentive contribution is based on achievement of **outputs** in key areas.

Transparency: We have pressed for increased transparency and information disclosure by the MDBs out of the conviction that public scrutiny of operations is one of the best ways to foster accountability and results. Further progress is necessary, but important achievements have been reached to date:

- All country assistance strategies for IDA countries are now disclosed to the public and posted on the World Bank's web site. These include CASs for Bosnia, Pakistan and India.
- All Poverty Reduction Strategy Papers are required to be released before any World Bank Board discussions; without such release, the Board will not discuss them.
- Recent reforms at the World Bank mandate release of: Chairman's Summaries for key issues (unless the Board objects); all adjustment loans for IDA countries (with voluntary release of all others); all OED evaluation reports (unless the Board objects); draft policies; Board work plans; and additional project preparation information. Previously, many of these documents were never released to the public.

- For the first time, at U.S. insistence, the draft IDA-13 recommendations of donors were posted on the World Bank website for public comment. The same practice was followed for the African Development Fund donors' recommendations.
- The IDB has created a special unit in charge of the Bank's civil society participation and has upgraded its website to improve accessibility, including immediate online access to entire environmental impact assessments for a number of projects.
- The EBRD is operating under a new public information policy that requires the Bank to disclose more information, including sector and country strategy papers, and to work more closely with NGOs and other stakeholders.
- The AsDB is also enhancing its transparency, with an expanded website, an improved public information center and a newly created NGO center. Looking ahead, the U.S. hopes to strengthen the AsDB's inspection panel, which is under review this year.
- The AfDB has a forward-leaning information disclosure policy that allows for all loan documents, country strategy papers and policy papers to be available to the public upon Board approval. At U.S. urging, it is continuing to develop its website and improve the timeliness of information distribution.
- The GEF is perhaps the most transparent of all, with virtually all GEF documents posted on the web, and NGO observers at Council meetings who speak on policy issues and projects.

Coordination: Given the limited supply of public funds and the overlap of individual MDB mandates, the U.S. has emphasized the importance of better coordination among development banks, especially on diagnostics, to remove unnecessary overlaps and to focus each institution on its comparative advantages.

The World Bank has signed memoranda of understanding (MOUs) with the African Development Bank, the Asian Development Bank and the Inter-American Development Bank. In addition, working groups have been established to intensify harmonization and convergence in MDB operations. These include efforts on project processing, procurement procedures, evaluation procedures, financial management and environmental assessments.

The World Bank is strengthening its collaboration the IFC through the creation of joint World Bank/IFC units, which have helped improve the impact of the World Bank Group.

CONCLUSION

We are making progress on our MDB growth agenda. While these gains are progressive and significant, they are only the beginning. The sheer scale of global poverty and unrealized human potential underscore the importance and urgency of improving the effectiveness of international assistance. Our challenge, going forward, will be to implement consistently our reforms measures over the long-term and have the courage of our convictions to take tough decisions -- concentrating our assistance on those countries with sound economic policies and good

governance practices, and withholding it when fundamentals are not right; focusing MDBs on measures to increase productivity and private sector job creation; insisting on accountability and measurable results; being more selective; and learning from both our successes and failures.
