International Monetary and Financial Committee

Eleventh Meeting
April 16, 2005

Statement by James D. Wolfensohn
President of the World Bank

IMFC Meeting April 16, 2005

Statement By James D. Wolfensohn
President of the World Bank

Introduction

1. 2005 is a milestone year for the international development agenda. It marks a third of the way to the target year of 2015 for achieving the Millennium Development Goals (MDGs). 2005 offers perhaps a last opportunity to make adjustments, and further commitments needed if the MDGs are to be met. Looking ahead, and with just a decade to go to 2015, achieving all the MDGs presents an enormous challenge. But we know that with the right policies and actions rapid progress is possible, and the success of the better performing regions and countries, including in Sub Saharan Africa, provides hope for others. If we fail to take the opportunity, the risks are great not only of not meeting the MDGs, but of failing to achieve the ultimate goal we all seek: the goal of a peaceful, prosperous and secure planet. 2005 is thus a year of great opportunity and also a year of grave risk.

2. In September, world leaders will meet in New York to review progress on the commitments they made in the Millennium Declaration adopted at the UN Millennium Summit in 2000, on the basis of the Secretary General's report. The recent report of the Commission for Africa, chaired by Prime Minister Tony Blair, gives a detailed assessment of progress and challenges in Africa – the continent most at risk of falling seriously short of meeting any of the MDGs. Tomorrow, at the Development Committee, we will be discussing the *Global Monitoring Report* (GMR), prepared by staffs of the Bank and the Fund with major inputs from the UN, WTO and other multilateral agencies, which gives a sobering assessment of progress in implementing actions and policies needed to achieve the MDGs, and what further action is now needed. That discussion, and today's discussion at the IMFC, are an important opportunity to shape and give impetus to the 2005 agenda and secure political commitment for achieving results.

3. As this will be the last meeting of this Committee that I will be attending as President of the World Bank I would also like to reflect a little on the critical importance of the strong partnership we have forged between the Bank and Fund in recent years, helping both institutions to do a better job in supporting development and poverty reduction, and in promoting financial stability.

The Global Economy

4. There are additional risks to progress towards the MDGs in the period immediately ahead from developments in the global economy. Over the last few years, developing countries in general have experienced a period of exceptional growth: 6.6 percent last year, compared with growth of 3.2 in high-income countries. This reflects

very strong growth among some of the developing world's largest countries (China, India and Russia grew 9.5, 6.8 and 7.1 percent respectively). Other developing countries in East Asia and Pacific, South Asia, and Europe and Central Asia also recorded strong growth; and in the Middle East and North Africa, Latin America and the Caribbean, and Sub-Saharan Africa, where the pace of the expansion was lower, it was much stronger than in the recent past. Following substantial structural and macroeconomic reforms during the 1980s and 1990s, trend growth rates in all developing regions have been rising.

5. But global growth is already decelerating with higher oil prices, rising interest rates and an end to the fiscal stimulus that boosted growth in the recent past, and this deceleration is projected to continue during the rest of 2005 and into 2006. Developing country growth will remain above 5 percent and per capita incomes even in the globe's poorest countries are expected to rise, but even so millions of people – particularly in Sub-Saharan Africa – will continue to live in poverty and the gap between their incomes and those of individuals living in high-income countries will grow. Moreover, there are significant risks that large global imbalances, further volatility in oil and metals prices or a change in investors' willingness to take on risk could result in a much more pronounced slowing of the global economy, with particularly adverse impacts on emerging market economies with significant levels of external short term debt, and on poor oil importing countries.

IMF support for Low-income Member Countries

6. In a year where our decisions and actions will be so crucial to success or failure in meeting the MDGs, it is timely to be reviewing the Fund's role in low-income countries. The Fund's role in low-income countries is a fundamental pillar of the evolving international development architecture. The Fund plays a central role, often jointly or in close cooperation with the Bank, in helping these countries make progress towards the MDGs. I hope the Committee will agree that it should continue to do so.

7. Let me say a few words on recent progress in collaboration between our two institutions in low-income countries. With changes in practices introduced in recent years, my sense is that there is now a good division of labor between the two institutions, based on complementary mandates and clear accountabilities in respective areas of responsibility.

8. **At the broader level**, the Bank and the Fund have jointly prepared the GMR which will be the focus of discussion at tomorrow's meeting of the Development Committee. There is strong agreement between the Bank and the Fund on the **five areas for progress in low-income countries identified in the GMR**:

- *Country Strategies*. Many of the poorest countries need to strengthen country-owned and -led poverty reduction strategies (PRSs), with better links with medium-term budgetary frameworks; more ambitious PRSs should provide the anchor for country actions to achieve the MDGs, and donors should act faster to align and harmonize their assistance around these strategies.

- *Investment Climate*. Many developing countries need to do much more to improve the environment for strong, private sector-led economic growth. Of particular importance in this regard are efforts to build deep, efficient and inclusive financial systems, strengthen fiscal management, with a focus on the structure of public spending; improve the enabling climate for private activity, by removing unnecessary regulatory and institutional constraints and strengthening economic infrastructure; and strengthen the quality of governance – upgrade public sector management and combat corruption.
- *Service Delivery*. We all need to do more to significantly scale up the delivery of human development services through a rapid increase in the supply of skilled service providers (health workers, teachers); increased and more flexible financing for these recurrent cost-intensive services; and improved governance along the service delivery chain to ensure that money produces results.
- *Trade*. We need bold actions to dismantle the barriers to trade to achieve an ambitious outcome of the Doha Round, which fully realizes its development promise, completing the Round no later than 2006, and by stepped-up assistance to poor countries to address behind-the-border constraints to their trade capacity, through investments in critical trade-related infrastructure.
- *Financing development*. Finally, the level and effectiveness of official development assistance needs to be increased significantly. In line with rising absorptive capacity, the GMR suggests that official development assistance (ODA) should be doubled from current levels, particularly to low-income countries and Sub-Saharan Africa, and that proposals for additional HIPC debt relief should be brought to closure in 2005—and without cutting into new ODA commitments.

9. **At the country level,** it is clear that if the MDGs are to be met countries themselves and institutions and partners providing support will have to scale up efforts on the ground. We have a sound basis for doing this, accepted by all partners, in **the Poverty Reduction Strategy (PRS) approach,** launched by the Fund and Bank some 5 years ago. Forty-seven countries are now implementing PRSs as country-led frameworks for development and achieving the MDGs, providing an anchor for both domestic efforts and external support. But in most countries the process needs to be deepened further, in particular by strengthening the link with medium-term expenditure frameworks and annual budgets, increasing transparency and better articulation of agendas for spurring economic growth. In many countries there is scope for using PRSs to assess options for accelerating policy reform matched by extra external assistance. In all countries, those providing assistance can and should do more to align and harmonize their assistance with country policies and systems. In the Bank we are continuing to support this approach, and to adapt our own procedures and instruments accordingly. We are currently undertaking jointly with the Fund a review of five years of implementation experience, seeking to draw lessons and identify good practices; to identify recommendations for strengthening implementation; and to clarify an appropriate framework for monitoring results. We are also currently completing a review of experience with our core instrument for supporting PRSs, the Poverty Reduction Support Credit (PRSC). I believe that the level of ambition

relative to PRSs can and must be raised: ambition on country actions to meet the MDGs, ambition on addressing capacity constraints and ambition on the volume and quality of financing needed to support country efforts.

10. **We need to act now to increase the amounts and quality of development financing**. The Monterrey Consensus represented an important milestone in framing the financing for development agenda. Since then, there has been considerable work on both assessing financing needs and on the different options for mobilizing development finance. The joint Bank-Fund paper prepared for the Development Committee on *Financing the Development Agenda* discusses the issues in more detail. Let me just highlight a few key messages. Developing countries can and must do more to mobilize domestic resources. In addition, many countries have been benefiting from stronger flows of inward investment (FDI) and remittances. But while FDI, remittances and exports are important sources of foreign exchange, they are no substitute for official development finance. Aid and other forms of development finance play a critical and special role, providing resources to support the public policy reforms and investments needed to underpin successful private sector development, economic growth and enhanced delivery of human services – and hence progress in meeting the MDGs. We must deliver on the promises of aid that have been already made, at and after Monterrey. In addition 2005 offers an important opportunity to raise sights higher for the future and to set goals on aid delivery, for example for 2010. We also need to continue to work on ways to increase the pool of resources for development through innovative mechanisms. These are all issues we will be addressing at tomorrow's meeting of the Development Committee.

11. In addition to increasing the volume of ODA **we have act at the country level to make aid more effective and more predictable.** As highlighted in the GMR aid is often fragmented and volatile, not well aligned with country priorities, and entails high transactions costs. Fortunately, these issues are now receiving more attention and progress is being made, but it has been slow and uneven. The Paris Declaration, which was adopted in March this year by 90 countries and 27 development institutions, set out 50 commitments to improve the quality of aid. The challenge ahead is to translate these agreements into results on the ground, and this will require concerted and cooperative efforts on the part of all. In country after country, and sector after sector, we have learned the power of aligning aid better with country priorities; strengthening and where possible using country budget and financial systems and processes; providing the assurance of predictable and flexible aid flows over a period of years so that countries can embark on long term programs, for example in education and health; and in some circumstances financing recurrent costs. Today only a very few donors are able to make medium-term aid commitments. I recognize that in many cases countries will only be able to implement this agenda in full if they can persuade parliaments to permit changes in the way their aid is delivered and accounted for. I hope we can agree on the importance of making the effort. Better alignment of aid with country priorities and the harmonization of aid practices should not be celebrated just in Mozambique, but should be the norm for all countries.

12. In countries not yet well placed to develop the PRS approach, we are working with other development partners **to improve the way we provide support to low-**

income fragile states, the so-called *low-income countries under stress* (LICUS). Effective international engagement with fragile states is essential for global security, for the well-being of the 500 million poor people living in these countries and for development in neighboring countries. There is increasing recognition by all that initial stabilization and peace-keeping efforts in the most fragile states need to be strengthened by building state capacity, state legitimacy, and viable economic recovery if these countries are not to slip back into conflict. Security and development linkages are very important in these countries. The Bank has collaborated with the UN Development Group to produce a new planning tool integrating political, security, economic and social issues in one unified results framework. In January, the Bank co-sponsored a *Senior Level Forum on Development Effectiveness in Fragile States* in London which helped develop a set of *Principles for Good International Engagement* in fragile states.

13. We are also looking at the way the Bank supports policy reform in low-income and other countries in our current **review of practice in the use of conditionality**. The conclusions of the review will be presented at the Annual Meetings. Although conditionality has been a controversial topic for many years, I believe that we are reaching a point where it may be becoming something of a misnomer. What we are now implementing in most countries is a partnership with a mutual commitment to support medium-term policy and institutional changes, in which the country decides and implements its own reform agenda, as in PRSs; and the Bank and IMF, and in many cases other agencies and donors also, advise on and support good policy reform agendas – with associated frameworks for measuring results – as appropriate with policy based loans and grants. These must be based on a few critical measures that embody real ownership and that will produce better results, rather than on an exhaustive list of conditions. These are issues on which the Bank and Fund have worked closely together in recent years, and will continue to do so in future.

14. The Fund and the Bank continue to work together on the **HIPC Initiative**, which has been a long-standing joint effort. Of the 38 potentially eligible countries, 27 have reached decision point and thus are eligible for debt relief. The August 2005 HIPC Progress Report will present a list of remaining potentially eligible countries likely to reach decision point. We have also recently finalized the joint **debt sustainability framework** for low-income countries. We hope this framework will bring the international donor community—and the recipient countries—together around a shared and coherent assessment of countries' financial needs and long term debt sustainability—a critical element in the context of efforts needed to reach the MDGs.

15. Looking forward, there is the issue of **additional debt relief for the poorest countries**. There are three main objectives that motivate proposals for additional debt relief **:** (i) to reduce the debt overhang in low-income countries consistent with long term debt sustainability considerations, and end the "lend and forgive cycle", which may cause some countries to stay in a continuous "debt trap"; (ii) to protect countries from exogenous shocks, which cause temporary payment difficulties as well as longer-term debt sustainability problems; and (iii) to provide debt service relief (equivalent to grants) as a means to augment the financing for the MDGs. Additional debt relief can make a positive contribution for many of the poorest and most vulnerable countries. I see three main benefits: immediate resources that debt or debt service relief would provide for

development needs; predictability that comes with the certitude of debt relief; and efficiency that comes with the flexibility and reduction in transactions costs.

16. But additional debt relief also needs to meet some important tests: (i) true additionality—it has to be fully financed and cannot be at the expense of other flows; (ii) equity—it is essential that additional debt relief be provided equitably across countries; (iii) efficiency—given the limited amount of new financing, debt relief needs to be provided where it is most needed measured by aggregate financing needs and debt sustainability, and linked clearly to standards of good governance; (iv) it should not undermine the financial viability of multilateral institutions, and (v) debt relief in the context of IDA should be supportive of progress made under IDA14 towards providing grants based on debt sustainability. The new debt sustainability framework can serve as a useful basis for guiding not only debt relief but the coordination of assistance by all donors and creditors to ensure long-term debt sustainability.

Other Areas of Bank-Fund Cooperation

17. In addition to our close cooperation on low-income countries, we are continuing to deepen Bank-Fund cooperation in a number of other areas.

18. We work together in supporting the **global trade agenda**, both in pressing the case for the bold actions needed to realize the promise of the Doha development round; and in supporting member countries in handling any transitional costs of trade liberalization and making the reforms and investments needed to take advantage of new opportunities.

19. We also continue our extensive cooperation on issues relating to **global financial stability and the integrity of the global financial system.**

- The joint Bank-Fund Financial Sector Assessment Program (FSAP) and the Reports on Observance of Standards and Codes (ROSC) are two central pillars of this effort. They provide a valuable framework for helping countries strengthen their financial systems and institutions, underpinnings that are critical to successful economic development and poverty reduction as well as to financial stability. In the five years since the programs were initiated, much has been accomplished. As of end-2004, about 120 countries – two-thirds of the membership – have participated in the FSAP program or agreed to participate in the near future. The ROSC exercise has also been remarkable, with 600 modules completed covering 120 countries from all regions of the world and at various stages of development. For the future, the key task is to help countries implement systematic follow up to these assessments – to build capacity and institutions and to mobilize technical and financial resources for the task.

- Anti-money laundering and combating the financing of terrorism (AML/CTF) also remains a special concern. Protecting national economies and financial systems against criminal abuse requires the adoption of highly elaborate and multi-sectoral prevention and control regimes. The Bank and

Fund have proposed steps to support international efforts to curb money laundering, including through close collaboration with the relevant international bodies, notably the Financial Action Task Force (FATF) and the UN bodies. With agreement a year ago that AML/CTF should become a regular part of the Bank's work and on the revised standard and its assessment methodology we have been working to expand our strategy for helping member countries enhance the integrity of public and private institutions through effective AML/CFT regimes, providing technical assistance to client countries through individual country and regional programs, and raising awareness through Global Dialogues.

Strategic Directions for the IFIs

20. Given the scale of the challenges and the central role of the Fund and Bank in helping meet them, it is more important than ever that the Fund and Bank be effective and efficient in what we do. So we should welcome an opportunity to reflect on our strategic directions. The GMR contains an assessment of the contribution being made by multilateral institutions, and many good suggestions for improvement. It also, rightly, stresses **the importance of strong and effective cooperation and coherence between institutions**, which is the final issue on which I would like to comment.

21. After ten years on 19th street, I am more than ever convinced that good partnerships on the development agenda can produce more than the sum of the parts. As the GMR stresses, the breadth and interconnectedness of the development agenda on the ground and at the global level places a high premium on partnership and coherence. The Bank has and is continuing to strengthen its collaboration with the IMF, the MDBs, the UN agencies, the WTO, other bilateral and multilateral institutions, with the private sector and with civil society organizations. I have devoted much effort over the last few years in trying to strengthen these partnerships between institutions. Although significant challenges remain, I believe this message is now taking hold across the international system. More than ever, successful development results depend on harmonization of efforts based on comparative strengths.

22. From my vantage point, I can say that the relationship between the Bank and the Fund has over recent years reached an intensity in the level of collaboration that is unparalleled either in our 60-year history as the Bretton Woods sisters or, even today, among other global and development institutions.

- Starting from Michel Camdessus' time as Managing Director, we have firmed up the foundations for an efficient division of labor between the two institutions, based on complementary mandates and clear accountabilities in respective areas of responsibility.
- At the annual meetings in Prague in 2000, Horst Koehler and I set out a shared vision for closer cooperation, based on national ownership of reforms, a coherent approach to supporting priorities based on an efficient division of labor, and the objective of focusing conditionality on measures critical to success.
- Almost five years on, with Rodrigo de Rato at the helm of the Fund, I am glad to report that both institutions have worked to implement this vision effectively and

in good faith. The principles and foundations that we have established for Bank-Fund collaboration will continue to serve well as we work together to help step up collective efforts towards the MDGs.

23. Going forward, I would like to leave the Committee with two reflections. First, it will be important for both institutions to continue to focus on their respective mandates and areas of comparative advantage as we continue to strengthen collaboration both on the global and thematic agenda and at the country level. Second, staffs of both institutions must continue to respect the immense accumulated wisdom and strengths of the other in their areas of comparative advantage. I hope the IMFC will continue to support further strengthening and deepening of this unique institutional partnership.

Conclusion

24. It has been a privilege to serve as an active participant in meetings of the IMFC since its creation five years ago. We have made much progress over that period, not least in enhancing cooperation between the two Bretton Woods institutions, thereby improving the effectiveness of both. The Bank is a remarkable institution, with a superb and dedicated staff, and its role in supporting development and the eradication of poverty has never been more important. I am confident that under the leadership of Paul Wolfowitz it will continue to rise to the challenge. And I am equally confident that you will find that he will make a continuing and valuable contribution to the future work of this Committee.