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Folder Title: Michael Bruno's chronological correspondence - May-Dec 1995

Folder ID: 1459983

Series: Michael Bruno's Chronological Correspondence File (Internal and External Chronological Files)

Dates: 05/01/1995 - 12/31/1995

Subfonds: Records of the Office of the Vice President, Development Economics and Chief Economist and later Senior Vice President, Development Economics and Chief Economist (DECVP)

Fonds: Records of the Office of the Chief Economist

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THE WORLD BANK

Washington, D.C.

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R1997-299 Other #: Box #: 394803B

Michael Bruno's chronological correspondence - May-Dec 1995

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**fr:
JUNE 95**

INTERNAL MAIL

JDW

The World Bank
Washington, D.C. 20433
U.S.A.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

Mr. James D. Wolfensohn

December 21, 1995

Bank-Fund Relations

Jim,

Rachel asked me to jot down some thoughts on Bank-Fund relations and how we might handle them under the new management structure.

My starting point is the brief we prepared for your lunch with Michel soon after your arrival in the Bank. At that time I stressed that the relationship between the Bank and the Fund is remarkably strong. We work closely together at the country level and share common views on matters of policy advice. However, there are also tensions and frictions. This is not surprising given our overlapping mandates. This overlap has increased since the early 1980s, as the Fund moved into longer-term adjustment programs (ESAF etc) and the Bank started providing short-term balance of payments support through adjustment lending. Tensions came to a head with the Bank's adjustment loan to Argentina in 1988 (over the Fund's objections). This led to the so-called Concordat of 1989 which still guides Bank-Fund relations.

As you know, there are pressures from the G7 to reduce the overlap between the two institutions. Indeed, in my view, a case can be made for merging the two institutions. But, short of this, we should be wary of accepting a simplistic division of labor. It is important, for example, that the Bank remains active in macro work, highlighting the links between macro and micro reforms (as we discussed in our workshop before your LAC trip). What we need to do is push for better collaboration and coordination between the two institutions. This is already happening in the areas of commodity price forecasts, public expenditure work, and now multilateral debt. But there is still a perception among many Bank staff that our relationship with the Fund is an "unequal partnership". We are more open with providing information and seeking the views of Fund staff, and often seem to get "steam-rolled" on policy issues.

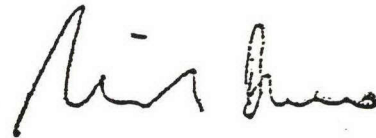
Against this background, I believe we need to establish clearer lines of communication with Fund management, to identify problem areas early and resolve them before they affect our day-to-day relations. Your regular breakfasts with Mr. Camdessus provide an important opportunity to build and maintain a strong personal relationship at the top of the two institutions. But we also need regular contact and clear lines of communication at different levels of management. Based on what I've seen of the way

we currently handle Bank-Fund relations, which is much more ad hoc than on the Fund's side, I would propose the following approach:

- We should reinstate your regular monthly lunches with Michel and senior managers from both institutions. From the Bank's side, the participants should include Gautam, Caio and myself. These lunches should have a clear agenda, prepared in consultation with Regional and Central Vice Presidencies, and a clear minute of what was discussed and areas for follow-up. We could also initiate regular meetings of senior managers, without yourself and Michel present, to follow-up on policy issues identified at the lunches and make proposals for their resolution.
- As the Bank's Chief Economist, I am formally responsible for relations on with the Fund on all general policy issues (country-specific issues are handled directly by Regional staff, although they often look to DEC for guidance and support on policy matters). However, in practice, the Fund has tended to access the Bank at whatever point it finds least resistance. This has contributed to the perception of an "unequal partnership". Now that we have the new management structure in place, it would be helpful if you could clarify my responsibility for Bank-Fund relations with Michel. It would seem logical for my counterpart in the Fund to be Stan Fischer (we know each other well and we have both worked on both sides of the street).
- Within DEC, my role on Bank-Fund relations will be back-stopped by the Director of Development Policy (Mark Baird). In addition, he will coordinate day-to-day relations with the Fund's Policy Development and Review Department (which is responsible for collaboration with the Bank on operational policy issues), the review of Fund policy papers, and the agenda for the senior management lunches and meetings. He will also liaise closely with EXC and OPR on the operational aspects of our relationship with the Fund (e.g., the ongoing work on public expenditure reviews and Policy Framework Papers).
- In addition, we need to establish clear lines of communication with the Fund on specific topics and issues. The current working group on multilateral debt, led by Masood Ahmed on the Bank's side, is a good example. But this needs to be sustained on a regular basis and extended to other areas. Within DEC, we will identify "point people" on issues of research, data, training and relationships with other international agencies. We will also coordinate similar initiatives in other parts of the Bank which deal with the Fund on policy issues (e.g., OPR, FPR). We will communicate these assignments to the Fund and ask them to identify appropriate counterparts on their side (from throughout the Fund, not just the Policy Development and Review Department).

- We are also looking at other ways we can improve collaboration between the two institutions. As you may know, we held a very successful workshop for Bank managers on Fund programs in November. This was coordinated by the Learning and Leadership Center, with inputs from both EDI and the IMF Institute. We propose to repeat this workshop on a regular basis. We are also talking with Fund staff about organizing an annual Bank-Fund retreat to focus on operational and policy issues. The first one is planned for mid-1996.

I would be happy to discuss these proposals with you. If you agree, we could take them up with the Fund at the next lunch. Before or after that lunch, you might also want to write to Michel setting out the proposed arrangements.

A handwritten signature in dark ink, appearing to read "Michael Bruno", with a stylized, cursive script.

Michael Bruno

cc: Mr. Kaji, Ms. Lomax.

The World Bank
Washington, D.C. 20433
U.S.A.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

December 21, 1995

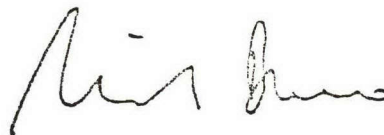
Mr. James D. Wolfensohn

Ref.: Robert Solomon's book: *The*
Transformation of the World Economy: 1980-1993

Dear Jim,

I am sorry not to have replied to you earlier. For some reason I only now received your note, via Israel! I don't know a thing about Bob Solomon's recent book. Is it something I should read, or should I ask for a review from my staff? Please let me know if I can be of assistance.

Thank you.

A handwritten signature in dark ink, appearing to read 'Michael Bruno', with a stylized, cursive script.

Michael Bruno

034

The World Bank
Washington, D.C. 20433
U.S.A.

JAMES D. WOLFENSOHN
President

95 DEC 20 AM 10:33

December 13, 1995

RECEIVED
DEVELOPMENT ECONOMICS
VP & CHIEF ECONOMIST

Mr. Michael Bruno
The World Bank
Room No. N-6043

Dear Michael,

Have you seen Bob Solomon's book? Is it any good? I have to drop him a note of thanks.



James D. Wolfensohn

~~Mark - I~~
faxed this
to Michael

Bulo:
Have you seen his?
as

Chon EXC

December 18, 1995

Ms. Rachel Lomax

Rachel,

Regarding your note of December 13 on outstanding correspondence from the President's Office, I have checked the outstanding DEC items and our records show the following:

- EXC Ref. #03902(received from A Choksi, 10/24): Forwarded to M .Malloch-Brown's office to handle, Oct. 24.
- EXC Ref #03151 (received from A. Choksi 9/25): Forwarded to M. Malloch-Brown's office to handle, 9/25.
- EXC Ref.#03067 (received from A. Choksi 9/20): Forwarded to M. Malloch-Brown's office to handle, 9/25.

In connection with the above correspondence please note that "standard" questions on structural adjustment are handled by EXT.

EXC Ref.#04311

An initial reply was sent to Maree Aniba. However, following an exchange of E-Mail/telephone conversations between you and Masood Ahmed and Alan Winters, and in view of the politically sensitive issue raised by Mickey Kantor on the position taken by WDR 95 on the use of trade sanctions to enforce labor standards, a second letter was prepared for Mr. Wolfensohn's signature and handcarried directly to you on November 22. (I understand that Maree Aniba did not get a copy of this letter but was alerted to the fact that a second letter had been delivered to you.) We are waiting to hear from EXC whether the letter has been signed.

If you have further questions please let me know.



Mark Baird
Acting Vice President, DEC

Attachments/-

CORRESPONDENCE MANAGEMENT FOR THE PRESIDENT'S OFFICE
CHORUS
External Correspondence Profile

Reference #: EXC-03902 ✓

For Action: Michael Bruno
VPU: DEC Room #: S-9035 Telephone: 33774

Log Date: 10/20/95 03:15:57 PM
Status: Open
Response Date:

CORRESPONDENCE DESCRIPTION:

From: Sisters of Mercy of the Americas, 09/28/95
To: Mr. Wolfensohn
Dated: 09/28/95
Topic: Structural Adjustment Programme

ACTION INSTRUCTIONS:

Due Date: 10/31/95

1. Please handle/respond on behalf of Mr. Wolfensohn and provide a copy to EXC.

SPECIAL INSTRUCTIONS:

According to EM from Masha, 10/24/95, correspondence has been rerouted to Mr. Bruno.

INFORMATION COPIES:

Please return to:
Maree Aniba, EXC, E1227, 84138

CORRESPONDENCE MANAGEMENT FOR THE PRESIDENT'S OFFICE
CHORUS
External Correspondence Profile

Reference #: EXC-03151

For Action: Michael Bruno VPU: DEC Room #: S-9035 Telephone: 33774	Log Date: 09/22/95 08:31:06 AM Status: Open Response Date:
---	---

CORRESPONDENCE DESCRIPTION:

From: Rebecca J. Tollefson To: Mr. Wolfensohn Dated: 09/16/95 Topic: Structural Adjustment Programs - Inflicting the poor with burdens

ACTION INSTRUCTIONS:

Due Date: 10/03/95

1. Please handle/respond on behalf of Mr. Wolfensohn and provide a copy to EXC.

SPECIAL INSTRUCTIONS:

this was forwarded to Mr. Bruno on 925 by Karen Umemoto

INFORMATION COPIES:

Please return to: Maree Aniba, EXC, E1227, 84138
--

DECLV A
Log # 006
rec'd (9/25)
→ External

CORRESPONDENCE MANAGEMENT FOR THE PRESIDENT'S OFFICE
CHORUS
External Correspondence Profile

Reference #: EXC-03067

For Action: Michael Bruno VPU: DEC Room #: S-9035 Telephone: 33774	Log Date: 09/18/95 06:03:51 PM Status: Open Response Date:
---	---

CORRESPONDENCE DESCRIPTION:

From: Dorothy Scott Smith To: Mr. Wolfensohn Dated: 09/14/95 Topic: Rejection of the LAP - Structural Adjustment

ACTION INSTRUCTIONS:

Due Date: 09/27/95

1. Please handle/respond on behalf of Mr. Wolfensohn and provide a copy to EXC.

SPECIAL INSTRUCTIONS:

this was forwarded to M. Bruno on 09/19

INFORMATION COPIES:

Please return to: Maree Aniba, EXC, E1227, 84138
--

DECLVP
log # 003
rec'd. 9/20
→ EXT.

CORRESPONDENCE MANAGEMENT FOR THE PRESIDENT'S OFFICE
CHORUS
External Correspondence Profile

Reference #: EXC-04311

For Action: Michael Bruno VPU: DEC Room #: S-9035 Telephone: 33774	Log Date: 11/09/95 09:55:54 AM Status: Open Response Date:
---	---

CORRESPONDENCE DESCRIPTION:

From: Mr. Michael Kantor, , Executive Office of the President, The United States Trade Representative To: Mr. Wolfensohn Dated: 10/31/95 Topic: The World Development Report 1995: 'Workers in an Integrating World'.	
--	--

ACTION INSTRUCTIONS:

Due Date: 11/30/95

3. Please prepare a response for Mr. Wolfensohn's signature according to the following instructions:

- a) Send the letter for Mr. Wolfensohn's signature back to Maree in E1227, together with the copy of the pink Log Sheet and incoming letter;
- b) Include two (2) copies of the response letter attaching a copy of the Log Sheet and the incoming letter which should show the bccs, drafter's ID and EXC log number (these copies will be stamped " (signed) JAMES D. WOLFENSOHN ";
- c) Once the letter is signed you will be called by staff from EXC to pick up the signed letter together with one "stamped" copy showing the bccs.
- d) VP Units are responsible for distribution of the original signed letter and the copies.

SPECIAL INSTRUCTIONS:

Due date extended -- (person responsible away). I requested them to send an acknowledgement letter.

INFORMATION COPIES:

Please return to: Maree Aniba, EXC, E1227, 84138
--

DEC VP
log # 024
rec'd 11/9

WDR 95
mw

The World Bank
Washington, D.C. 20433
U.S.A.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

Mr. James D. Wolfensohn

December 12, 1995

1997 World Development Report: Topic Selection and Endorsement

Jim,

It is time for us to make a decision on the topic for the 1997 *World Development Report*. As you know, the WDR is the Bank's flagship publication with a distribution of 150,000 copies and an even wider readership. The selection of the topic involves extensive consultations within the Bank and, informally, the advice of a few prominent external advisors. A number of topics have been around for several years, and many are good candidates; for example, gender in development; aid effectiveness; the role of institutions; the changing role of the state; information, technology and development, etc. The choice of what to do is really more a decision of what to do today and what to wait for tomorrow. It is a difficult choice for two main reasons. First, the WDR should be a clear, succinct and synthetic statement of a major issue in development. This means that, in preparing the WDR, the team has to rely mainly on pre-existing material. There is time to select, integrate and synthesize but hardly any for new research. Thus, lack of previous work--done in-house--is a major roadblock in topic selection. Second, as the Bank's flagship publication, the WDR should address an overarching theme for the Bank, one that highlights the Bank's contribution to development. The most successful WDRs are major turning points on an ongoing debate (for example, the 1991 WDR on *The Challenge of Development*) or are themselves "the" reference point in that debate, marking clearly the Bank's intellectual position (for example, the 1990 WDR on *Poverty*).

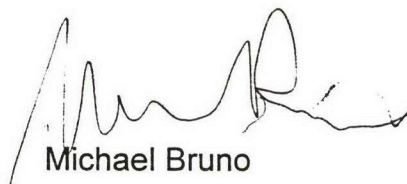
This year we focused on three themes for which we prepared tentative outlines. (Preparing these outlines is critical for, in the process, one gauges the depth of material available, the robustness of arguments and, not less importantly, the political implications of the main messages.) As described in the note attached (which I sent to those who helped us in the selection process) the three themes were:

- The changing role of the state;
- Aid effectiveness;
- The new regionalism (post-Uruguay Round)

We chose to present to you as our preferred topic for the 1997 WDR *The Changing Role of the State*. As you know, the Bank is viewed in some quarters as being anti-government and in others as still being too pro-public sector. This WDR would provide us with an opportunity to set the record straight and show both where we think the state has a role in the provision of goods and services and where we think development would be better served by leaving the task to the private sector. Such a report would go well beyond basic economics. It would also deal with the challenging issues of political economy and institutional reform. We have worked on these issues but more will be required -- and we intend to put DEC resources at work in anticipation of this task. Finally, and perhaps most importantly, this WDR will have important implications for the World Bank and the donor community more generally as we collectively try to help countries strike the right balance between public and private action and responsibility.

I hope you agree with this choice and support us in our effort. We are now searching for an appropriate task manager. Following a long-standing tradition, and if you agree, you will announce both the topic and the manager sometime in January. We will then gladly prepare a draft statement for your review.

Thank you,



Michael Bruno

cc: MDs, Ms. Lomax

attachment

OFFICE MEMORANDUM

DATE: November 22, 1995

TO: Distribution

FROM: Michael Bruno, DECVP *mb*

EXTENSION: 33774

SUBJECT: 1997 World Development Report

This is to advise you where we stand regarding the 1997 World Development Report. I am grateful for the inputs from many of you in this process.

After extensive consultations and much thought, we are recommending *The Changing Role of the State* as the topic for the 1997 WDR. A wide range of topics have been suggested and were considered, many more than in the last two previous years.¹ Three clusters stand out. One, a cluster on issues of aid effectiveness, project implementation and the role of institutions in development. Two, a cluster on issues of growth, poverty and environmental sustainability. Three, a cluster on public expenditures, decentralization and targeting of public assistance. Interestingly, all three clusters are related and speak rather directly to the role of the Bank in delivering development impact. They also concern the changing role of the state.

Perhaps more so than past WDRs, this topic is at once an area where the Bank has had, on the one hand, a long and varied experience -- indeed, we have been a part of "the changing role of the state" as long as we have been in operation. Yet it is also an area that we have failed to address systematically until quite recently. Nearly all past WDRs dealt with parts of this issue, and especially the 1983, 1988, 1991 and 1994 WDRs on *Management in Development*, *Public Finance in Development*, *The Challenge of Development* and *Infrastructure for Development*. Yet we have not dealt directly with the theme; we have not presented our view of how public action and institutions have been *and can be* used to best promote shared and sustained development.

¹ They include *Information and development*; *Industrial pollution*; *Public expenditures*; *Rural development*; *Children*; *Aid effectiveness*; *Income distribution*; *Poverty, environment and growth*; *Savings*; *The changing role of the state*; *Education*; *Project impact and evaluation*; *Gender and development*; *Laggards in development*; *Capacity building*; *Institutional development*; *Civil society*; *Private capital flows*; *The economic effects of corruption*; *Regionalism, post Uruguay Round*, to cite only some of them.

As you know, the Bank is viewed in some quarters as being anti-government and in others as still being too pro-public sector. This WDR would provide us with an opportunity to set the record straight and show both where we think the state has a role in the provision of goods and services and where we think development would be better served by leaving the task to the private sector. Such a report would go well beyond basic economics. It would also deal with the challenging issues of political economy and institutional reform. We have worked on these issues but more will be required -- and we intend to put DEC resources at work in anticipation of this task. Finally, and perhaps most importantly, this WDR will have important implications for the World Bank and the donor community more generally as we collectively try to help countries strike the right balance between public and private action and responsibility.

The choice of topic was a difficult one. I have consulted with many of you on the advisability of proceeding with a WDR on *Aid Effectiveness - Development Assistance*. We in DEC are in the process of producing research that I think will be innovative, judicious and operationally focused on key aspects of this topic. In about a year we will hopefully be in a position to write a convincing, empirically grounded analysis on how to improve the development impact of aid. Why then not do a WDR on this central aspect of our work? Because our conversations have persuaded me that we would face questions of credibility (can we evaluate ourselves?), of commitment (can we speak as one voice without diluting much of the message?) and of breadth (can we address convincingly the many aspects of aid?) which the WDR team would not be capable of answering without defacing the character of what is a WDR. Certainly we must do more work on institutions and on the political economy of development and sustainability of reform. There is a good chance that with the added support of this work we will be ready, in a year or two, to tackle this thorny issue from a more complete, conceptual and yet policy-linked perspective. Meanwhile, if the fruits of our work justify a major Bank statement on aid effectiveness, we *will* produce such a document for your appreciation.

Likewise, we have debated the theme of *Growth, poverty (inequality) and environment*. Again, this is a topic on which DEC is engaged in a major research effort. Our sense is that it is better to wait and see the product of this effort before launching a WDR on this topic. Admittedly, there is already a vast literature on each one of the components of this topic, and there is also material in the Bank that attempts to integrate them from the perspective of development. However, most of this material is not the product of research and is not based on the kind of careful empirical measurement that the new research is based on; it is, to be sure, useful material but mainly as a synthesis of other work and we should aim for more definitive answers about the linkages among growth, poverty and environment before writing a WDR.

A third topic that was debated was Regional Integration. This had several attractions: it is of widespread and immediate policy relevance; there have been several recent developments in thinking on the topic, although opinions remain diverse and analytically uncertain, so that a considered evaluation of the evidence could be valuable; much research is under way inside and outside the Bank; and it would offer scope for cooperation with other international institutions. Nonetheless, I felt that the topic was too narrow for a WDR and hope, instead, to produce a Policy Research Report over the next two years.

I hope that you agree that *The Changing Role of the State* is a pressing issue, one where the Bank should have a clear and informed position. We will need all your support to carry through with this task.

Thank you.

Distribution: RVPs, Chief Economists, Country Directors, Linn (FPRVP), Choksi (HCOVP), Rischard (FPDVP), Serageldin (ESDVP), Ahmed (IECDR), Baird (DECVP), Gelb (WDR), Ingram (RAD), Squire (PRDDR), Thomas (EDIDR), Vieira da Cunha (DECVP), Wilson, McCalla, Binswanger (AGRDR), Pouliquen (TWUDR), Petit (ESDAR), Cohen (ESDVP), Steer (ENVDR), Malloch-Brown (EXTDR), El-Ashry (GEF), Perlin, Rao (FSDDR), Stern (IENDR), Iskander (PSDDR), De Ferranti (HDDDR), Husain (ESPDR), Picciotto (DGO), Anderson (IENDR), Devarajan (PRDPE), E. Jimenez (PRDPH), D. Dollar (PRDMG), Iqbal (EA3CO), Jechoutek (IENPD), Johnson, I. (GEF), Kleynhoff (FPFVP), Leipziger (LA1DR), Messenger (ASTDR), Muis (CTRVP), Rogerson (AF3DR), Winters (IECIT).

The World Bank
Washington, D.C. 20433
U.S.A.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

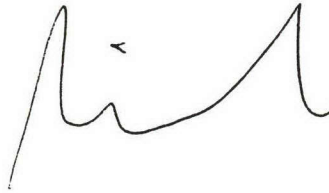
Mr. James D. Wolfensohn

December 7, 1995

Dear Jim:

I thought you would like to see this note of appreciation for the Bank's work.

Sincerely,

A handwritten signature in black ink, appearing to be 'Michael Bruno', written in a cursive style.



Record Removal Notice

File Title Michael Bruno's chronological correspondence - May-Dec 1995		Barcode No. 1459983		
Document Date 12/06/1995	Document Type Memorandum			
Correspondents / Participants From: Sergiy Kulyk, Executive Director To: Mr. Vinod Thomas, Director Economic Development Institute				
Subject / Title Letter from Vice Prime Minister Shpek				
Exception(s)				
Additional Comments Declassification review of this record may be initiated upon request.		The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information or other disclosure policies of the World Bank Group. <table border="1"><tr><td>Withdrawn by Salma Berrada</td><td>Date April 29, 2025</td></tr></table>	Withdrawn by Salma Berrada	Date April 29, 2025
Withdrawn by Salma Berrada	Date April 29, 2025			

UNOFFICIAL TRANSLATION FROM UKRAINIAN BY THE EMBASSY OF UKRAINE TO THE USA

CABINET OF MINISTERS OF UKRAINE

#27-3067/9

Mr. V. Thomas

Director, Economic Development Institute

The World Bank

Washington DC

1995

November 13,

Dear Mr. Thomas:

I am very glad to have this opportunity to express deep appreciation of your fruitful assistance to Ukrainian State in retraining of the Central and Local Governments officials as well as for your efficient and wide economic knowledge dissemination program for members of the Parliament of Ukraine and various professionals.

The Government of Ukraine appreciate the important efforts of the Economic Development Institute in providing the knowledge of basic market economics and disseminating the acquired experience of market reforms of many countries. Having started our program of macroeconomic stabilization in the fall of 1994, we consider the investing in a personnel to be able to implement reforms in Ukraine as one of the important challenges of reform process.

I express the hope on continuing cooperation with the Economic Development Institute on these matters. It is important to secure the programs of retraining to include courses of various duration in micro- and macroeconomics, financial and project analysis, project management, as well as seminars on policy instruments and transitional economies issues. I would like to appreciate especially your efforts in establishing training courses for the key economic ministries officials abroad

in particular at the facilities of the Joint Vienna Institute.

The important contribution in upgrading the level of knowledge of our officials would be the dissemination of the training materials in market economics and financial analysis. We would like also to disseminate monthly analytical bulletin on economic development. We may secure the help of the Joint Training Center established by the EDI and the Ukrainian Academy of State Administration under the President of Ukraine and the help of personnel training departments of the Cabinet of Ministers, Ministries and other governmental agencies in preparing and disseminating mentioned materials.

Sincerely,
Deputy Prime Minister

R. SHPEK



19

№ 27-8087/9

13 листопада 1995 р.

пану В. Томасу
Директору Інституту
економічного розвитку
Світового банку,
Вашингтон, О.К.

Шановний пане Томас!

З великим задоволенням звертаюсь до Вас із словами щирої подяки за Вашу піддаву допомогу українській Державі у справі перепідготовки кадрів державних службовців центральних міністерств і відомств, місцевих органів державної виконавчої влади та Вашу ефективну і широку програму економічної просвіти для народних депутатів України, представників різноманітних професій.

Український Уряд усвідомлює значення роботи, що проводиться Інститутом економічного розвитку, щодо поглибленого вивчення основ ринкової економіки та набутого досвіду багатьох країн світу з ринкових реформ. Розпочавши восени 1994 року програму макроекономічної стабілізації, ми бачимо одне із важливих завдань нашого реформування у створенні надійного кваліфікованого кадрового потенціалу, який забезпечуватиме проведення економічної реформи в Україні.

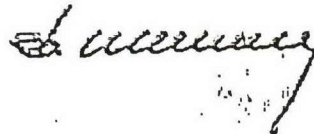
Маю надію, що співробітництво з Інститутом економічного розвитку буде продовжуватись подальше. Важливо, щоб коло програм економічного навчання охоплювало різноманітні чи напрямками і термінами курси з питань макро- та мікроекономіки, фінансового аналізу, управління інвестиційними проектами, а також семінари з проблем перехідної економіки та вибору інструментів економічної політики. Окремо хотів би підкреслити Вашу роботу по організації освіти провідних фахівців економічних установ за кордоном, зокрема в Світоглядному Підприємству Інституту.

Важливий внесок у справу підвищення рівня підготовки спеціалістів мав би внесок розглядаючих наочальна методичної літератури з питань ринкової економіки та фінансового аналізу і щомісячного аналітичного журналу з проблем економічного розвитку за допомогою Спільного економічного навчального центру (створеного Інститутом економічного розвитку на базі Української академії державного управління при Президентові України) та відділів з підготовки кадрів Кабінету Міністрів, міністерств та відомств.

З повагою

Віце-прем'єр-міністр України

Членство в кабінеті

 Р. ШПЕК

OFFICE MEMORANDUM



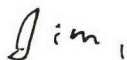
DATE: November 8, 1995

TO: Mr. James D. Wolfensohn

FROM: Michael Bruno 

EXTENSION: 33774

SUBJECT: **Inauguration of the Eighth Annual Conference on Development Economics**



I would like to take this opportunity to invite you to inaugurate next year's Conference on Development Economics at 9:00 a.m. on Thursday, April 25, 1996, and to stay for the keynote address. The conference will be held on April 25 and 26, 1996 in Washington D.C.; the themes are:

- ▲ Legal Systems and Economic Development
- ▲ Alleviating Poverty: Targeted Programs and Rural Credit
- ▲ Banking Failures: Crisis or Opportunity for Reform
- ▲ International Trade: Labor and Environmental Standards.

Gregory Ingram or I would be happy to provide further details about the conference and work with your office to prepare your inaugural comments.

cc: Rachel Lomax, Atsuko Horiguchi, Allison Tsatsakis, EXC

OFFICE MEMORANDUM

DATE: October 24, 1995

95 OCT 25 AM 9:34

TO: Mr. James D. Wolfensohn, EXC

RECEIVED
DEVELOPMENT ECONOMICS
V.P. & CHIEF ECONOMIST

FROM: Mark Baird, Acting DECVP

EXTENSION: 31666

SUBJECT: **Relations with WTO**

Mr. Bruno had two meetings with Jesús Seade, Deputy Director-General of WTO, over the Annual Meetings period. The first, which was also attended by Mr. Boorman (IMF) and his staff, constituted the first meeting of the Working Group on Coherence in International Policy Making. Mr. Seade seemed surprised that the Bank and the Fund had done any thinking on this matter, and asked to see their preliminary internal documents. These have now been sent to him. He promised that the WTO would respond setting out their view of coherence relatively soon. The deputies to the working party have been asked to produce a draft report by March 1996, emphasizing the practical issues of coherence that could be addressed, and the Working Group will meet again in April 1996. The Fund and the Bank expressed the hope that the Working Group would complete its work by that time, but Mr. Seade's view was that it would probably take significantly longer.

The second meeting was on the Cooperation Agreement between the Bank and WTO. This was a constructive meeting which made significant progress on a draft agreement. However, major differences remain between the Bank and WTO over access to the Development Committee and to the Bank's Executive Board. Mr. Seade felt that the member governments of WTO would be unable to agree to any Cooperation Agreement which did not give WTO access to restricted sessions of the Development Committee and to at least some country-specific sessions of the Executive Board. Both issues caused the Bank side some difficulty--the Development Committee because the new format does not appear to be consistent with offering privileged status to WTO, and the Executive Board because the Board itself showed some reluctance to admit WTO to country-specific meetings. It was agreed that these matters would be reviewed after the WTO had discussed them with the Fund, but we understand from the Fund that, when they did so, the Fund was similarly unencouraging.

We have not yet heard from WTO how they wish to proceed following the meetings. However, it now seems clear that we cannot complete the Cooperation Agreement by November as originally planned. Mr. Bruno has asked IEC staff to keep in contact with WTO and to explore with them ways in which the various matters might be resolved. We will keep you informed.

c.c. Messrs./Mss. Frank, Kaji, Sandstrom, Lomax, Horiguchi (EXC),
Bruno (DECVP) o/r, Ahmed, Winters (IECIT)

Cham SW

The World Bank
Washington, D.C. 20433
U.S.A.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

Mr. James D. Wolfensohn

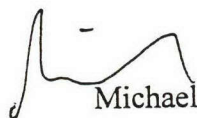
October 18, 1995

Your Visit to Russia and Hungary

Jim,

It was good to have the opportunity to discuss with you some of the issues in transition, as we see them. Following your request, I am sending you three notes linking messages from the workshop to specific country aspects. There are notes on Russia and Hungary and one on pension reform. I am glad you will participate in the round-table at the *Collegium Budapest*. The subject of pension reform is very much at the forefront of the discussion on "the new social contract." It is an area where we have done some work and I would like to share with you some thoughts I had, in anticipation of that discussion. Please give Prof. Kornai my best regards.

Wishing you and Elaine a good trip--I am sorry I could not join you this time,


Michael Bruno

Attachments/3

cc: Messrs. Kaji, Thalwitz, Ms. Lomax

RUSSIA

- The Soviet economy was in decline for 20 years before *glasnot* and *perestroika*. Problems did not begin with Mr Gorbachev, or the arrival of the IMF and the World Bank. On official data GDP has fallen to half its 1989 level.
- Liberalization in 1992 was partial. There was no policy *big-bang* and the results show it: Stabilization begins to take hold only in 1995 and at 5% a month inflation is still high.
- The budget improvement is impressive. But it results partly from short-term expedients (for example, not meeting expenditure commitments to basic education). Stability is fragile.
- There is a need to re-assert authority over key public resources, notably over *Gazprom*. Elimination of 1% of GDP worth of tax privileges for *Gazprom* (de-facto controlled and partly owned by Mr Chernomyrdin) would do much to improve the fiscal outlook.
- Mass privatization privatized over 16,000 of about 30,000 medium and large enterprises and between 50 and 75% of small businesses. There is a group of property owners who support the market and resist backsliding. They make reform in Russia close to irreversible.
- Privatization was mainly to existing managers for free or for nominal prices. The public perceives the program as unfair. Vouchers lost value early in the process (some were exchanged for a pair of boots).
- Insiders are not good owners. They do not have the skills to restructure their firms nor the will to fire redundant workers. They erect barriers to secondary trading of shares. So far, one can see no difference between the old state and the new privatized firms. And surveys show that units sold at competitive prices perform better than those that were given away.
- Corruption is widespread. At all levels bureaucrats seek pay-off and re-create red-tape. Private "contract enforcement" through organized crime is extensive. The huge benefits collected from control of state property hampers improvement, as does the low pay of public officials, including the police, and the underdeveloped legal institutions.

- 30% of the population is now poor. The losers are children and older workers with little education. The winners are younger, more educated, more dynamic—and those with better connections.
- Targeted social assistance is a priority; but there is no income testing and the motivation and capacity of government agencies is low. Health services have deteriorated. The life-expectancy of mature males has fallen dramatically to levels far lower than in China.
- Reform has yielded political freedom and democratization may spur economic change. Yet Russians are pessimistic. They may consider their situation tolerable but few consider the present to be better than the past. A majority does not expect rapid improvement.
- Transition is a deeply political process and the political problem is at present the most serious one. Political volatility has been high and will continue. As elections—December 1995 for Parliament and June 1996 for the presidency—approach, campaigning will crowd out the Government's ability to focus on reforms. The opposition parties are expected to make significant gains.
- Large Bank lending was demanded by the G-7 and by parts of the Russian government. But neither our Board nor our client speak with one voice. There are 19 loans approved totaling \$4.6 billion. Only 30% is disbursed (mainly the 2 adjustment operations) and getting results on the ground has been even more difficult.
- Implementation capacity is weak; we care how our money is spent—and our procedures prevent officials from rewarding their friends and making some easy money. Our loans have supported reform.
- Bank operations should focus on quality with a strong analytical content and impact. A little humility and a lot of pragmatism are in order—there are no blueprints and we are learning as we go along. We need to devote more attention to building effective institutions—and whether or not we lend, we can still educate and be educated.

HUNGARY

- **Reform:** Cautious, gradual reform marks post-1988 Hungary. There is no policy *big-bang* and the contrast with Poland is remarkable: Poland started later and from a worse position, but it has overtaken Hungary. It already enjoys some of the benefits of quick and decisive reform; at end-1995, the Polish economy is expected to be 16% larger than at end 1992; Hungary's GDP is expected to be 1% smaller.
- There has never been a real crisis but, also, no major policy breakthrough. Politicians don't lack understanding of the various macro and structural problems. What they lack is a clear perception of the magnitude of the problem and the urgency with which it must be tackled.
- The Mexican crisis prompted action; the response was partial and, again, tentative. We, the IMF and the market see Hungary as more vulnerable than pre-crisis Mexico. Why? Because debt is 70% of GDP, debt service eats up more than half of export revenue, the current account deficit will probably be around 9% of GDP for 1995 and the consolidated fiscal deficit, probably around 7% of GDP when taxes are already 50% of GDP. There is considerable domestic debt at very high real interest rates (interest payments on the government debt are 7% of GDP and may be 9-10% of GDP at end-1995). The financial system is fragile. But, mainly, there is apprehension because there is no history of decisive action.
- Messrs. Bokros and Suranyi say that they have done a lot; that without these actions the situation in 1994 would have exploded. This is, to be sure, true. But the actions did not correct for the pre-existing problems and they may be easily reverted. The IMF is easing its position a bit and agreement with the IMF is essential. *This calls for substantial upfront action to overcome the credibility gap.*
- **Privatization:** In 1990, Hungary had 1,832 medium and large enterprises on the books of the State Privatization Agency (SPA), and another 600 enterprises not managed by the SPA. By the end of 1994, 871 been privatized, 620 fully. By Government calculations, 48 % the medium and large enterprises entrusted to the SPA have privatized. In addition, close to 10,000 small scale units (perhaps 60 % of the total stock) have been sold leased, with managers of the units becoming the new owners in half the cases. At present, a bit more than half of all enterprises previously owned by the state have passed to private hands.

- Nonetheless, Hungary's divestiture program has to be judged as modest in both scope and pace. Why? In the late 1980s and early 1990s, a substantial set of assets was lost to "spontaneous privatization," in which *nomenklatura* managers obtained a firm's assets while leaving the liabilities to the state. This soured the public on privatization, and led the selling authorities and their supervisors to exercise greater caution and stress transparency -- all of which greatly slowed the sales process.
- Moreover, Hungary has relied on direct sales as its main divestiture method. It has eschewed vouchers. When faced, on several occasions, with a slowdown in sales, it has tried to use credit schemes, an employee stock ownership program (ESOP), and various administrative measures to speed the process, with only modest success.
- The socialist-liberal coalition has not been enthusiastic about privatization of the large industrial and service firms, and alienated investors earlier this year when it canceled a signed contract with a foreign purchaser of a major Budapest hotel group. On the other hand, the Government has continued a policy of involving the private sector in infrastructure that puts Hungary in the forefront of transition countries regarding the private provision of public services. Several major infrastructure transactions are presently being negotiated -- in each of these sectors, the private sector will hold a concession, supply a BOT, or obtain a minority.
- **Safety net:** As elsewhere in the transition, poverty has increased in Hungary but comparatively by a very small amount. This is the good news. The bad news is that Hungary spends more than it can afford on social services, pensions and transfers. The tax burden is half of GDP and the ratio of active to retired workers is 2:1. There is little left for investment and growth. Hungary needs to reduce social spending while managing very high social expectations.

HUNGARY: *Reforming the pension system*

The problem. Hungary's labor force is about 5 million people; the number of retirees is 2.6 million and at least 1.9 million receive other forms of social assistance. The average pension is 66% of the average net wage. Pension spending topped 10% of GDP in 1994. Public transfers, including subsidies but excluding interest payments on government debt, summed to 28% of GDP. In Hungary, as elsewhere in central and eastern Europe, people were generally eligible for an old age pension at age 55 (women) or 60 (men). Significant groups received a pension even earlier; and pensions were paid to people even if they continued to work. Since the start of the reforms, the number of pensioners has increased further because many older workers (in Hungary more than ten percent of older workers) have been allowed to retire early. The resulting problems are that (a) pensions are paid to too many people, (b) pension spending is too high, given the need to reduce public spending to allow private investment to grow. Reducing pensions and reforming the pension system creates a political problem because it takes away at least part of people's inherited entitlement—and forces them to confront realistic but unwelcome expectations.

Approaches to a solution are twofold:

- reform the state pension scheme,
- take early steps to encourage the development of a private pension sector.

A strategy for pension reform should recognize that pensions have three purposes:

- they should relieve poverty by ensuring pensioners at least a minimum standard of living;
- they should allow people at least partially to protect their customary living standards by redistributing from their middle years to themselves in old age;
- they should offer a measure of insurance, for example against premature widowhood or permanent health problems.

To achieve these three goals, *a pension scheme will generally have three pillars*: a state scheme, at least part of whose purpose is poverty relief; a mandatory private scheme; and a voluntary private scheme for individuals who wish to make additional provision for their old age.

Reforming the state scheme. The key point is that introducing private pensions is no substitute for direct reform of the state pension scheme. Specific policies include:

- Raise the age of retirement. This is politically difficult but must be done. The legislation in Hungary is currently under discussion.
- Introduce a retirement test for the receipt of an old age pension, i.e. pay pensions only to people who have retired not (as at present) to those who continue to work.
- While the fiscal crisis lasts, pay the state pension at a parsimonious flat rate per person, rather than, as currently, as a fraction of their previous earnings. Whether the earnings-related state pension is brought back once the economy is in better shape is a matter of (i) continuing fiscal prudence, and (ii) democratic decisions taken in Hungary.
- Reduce and rationalize access to disability pensions.

The Bank is working with Hungary on pension reform in the context of the proposed *Public Sector Adjustment Loan* (PESAL). There are several technically feasible solutions and because this is a politically loaded issue we should tread carefully and with due pragmatism.

Introducing private pensions. Private pensions help spur capital markets and increase the flexibility of labor markets.

- Work on the design of mandatory private pensions (the second pillar) and voluntary schemes (the third pillar) should proceed with some urgency.
- The starting point is to develop both the financial market institutions and the necessary financial market regulation, to protect consumers in an area where they do not have sufficient information to protect themselves and where there is a clear public interest and/or guarantee.
- If spending on the state pension is reduced, it will be possible to reduce contributions to the state scheme, so that workers will be able to afford to make contributions also to a private scheme.
- Mandatory private pensions can be organized on an individual basis or through occupational schemes. A case can be made for either; a case can be made for having both, allowing more choice both to individuals and industries. This is another area of debate where pragmatic solutions should be sought with attention to the costs of administration.

SOURCES:

Nicholas Barr (ed.), *Labor Markets and Social Policy in Central and Eastern Europe*, Oxford University Press for the World Bank and London School of Economics, 1994, Chapter 9.
Estelle James, et al, *Averting the Old Age Crisis*, Oxford University Press for the World Bank, 1994.

The World Bank
Washington, D.C. 20433
U.S.A.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

Mr. James Wolfensohn

September 29, 1995

Jim:

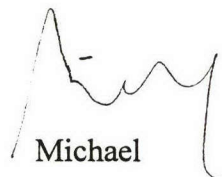
The attached draft for the Annual Meetings retains your structure and much of your words. We have tried to bring out the main messages and to shorten it--it is still too long, about 45 minutes.

As it stands, there are four main messages:

- (1) The need for a "new compact" on development assistance: for donors to ensure adequate resources (IDA) and for recipients and the Bank to ensure they are used more effectively.
- (2) The need to approach development in an "integrated" way, bringing all the different pieces together.
- (3) The Bank's need for new partnerships.
- (4) The need to change the Bank's culture and gear it to results and excellence.

The draft reflects inputs from Russ Cheetham, Gautam Kaji, Rachel Lomax, Mark Malloch-Brown and me, after reading your draft. The version you have now was put together by Gerry Rice, Lyn Squire, and Vinod Thomas.

Please call me over the weekend if you have reactions or want further work at (202) 337-4840.



Michael

Attachment

cc: Madam/Messrs. R. Lomax, G. Kaji, R. Cheetham, M. Malloch-Brown, M. Strong.

The World Bank
Washington, D.C. 20433
U.S.A.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

September 8, 1995

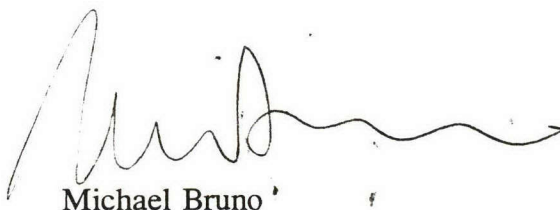
Mr. James D. Wolfensohn

Jim,

Re: World Bank Office in Geneva

This refers to your query as to who would be involved in a decision to reopen the Geneva office. The responsibility for WTO rests with the Development Economics Vice Presidency. The responsibility for relations with the UN system rests with the Human Capital Development and Operations Policy Vice Presidency (Mr. Choksi). Given the importance of the Bank-WTO relationship, I would suggest that we undertake to monitor the situation, in consultation with Mr. Choksi, and make a recommendation to you, should a change in policy be necessary.

Regards,



Michael Bruno

cc: Mr. Choksi

CORRESPONDENCE MANAGEMENT FOR THE PRESIDENT'S OFFICE

CHORUS

Internal Correspondence Profile

Reference #: INT-00222

Log Date: 09/05/95

Status: **Active** (Open, Closed but not filed, Filed, Active)

CORRESPONDENCE DESCRIPTION:

From: Michael Bruno VPU: DEC Development Economics
To: Mr. Wolfensohn
Dated: 08/31/95
Topic: World Bank Office in Geneva

REMARKS:

JDW responded a note to Bruno "Thanks. Who is involved in making the decision?" dated 09/05/95.

INFORMATION COPIES:

☐ Save & Exit ☐ Exit ☐ New Internal Correspondence Log

Please return to:

Lai-Foong Goh, EXC, E1227, ~~31383~~ 80388



Record Removal Notice

File Title Michael Bruno's chronological correspondence - May-Dec 1995		Barcode No. 1459983
Document Date 08/31/1995	Document Type Letter	
Correspondents / Participants From: Michael Bruno To: James D. Wolfensohn, President		
Subject / Title Re: World Bank Office in Geneva		
Exception(s) Corporate Administrative Matters		
Additional Comments		The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information or other disclosure policies of the World Bank Group.
		<table border="1"><tr><td>Withdrawn by Salma Berrada</td><td>Date April 29, 2025</td></tr></table>
Withdrawn by Salma Berrada	Date April 29, 2025	

THE WORLD BANK GROUP

ROUTING SLIP		DATE: August 4, 1995	
NAME		ROOM. NO.	
Mr. S. Lateef, Acting Director, IEC		S9-065	
cc.: Mr. Alan Winters		R2-033	
☐	URGENT	☐	PER YOUR REQUEST
☐	FOR COMMENT	☐	PER OUR CONVERSATION
☐	FOR ACTION	☐	NOTE AND FILE
☐	FOR APPROVAL/CLEARANCE	☐	FOR INFORMATION
☐	FOR SIGNATURE	☐	PREPARE REPLY
☐	NOTE AND CIRCULATE	☐	NOTE AND RETURN
☐		☐	
RE: Attached			
REMARKS: Sarwar, Could IEC please prepare a response to Mr. Wolfensohn? I suggest the response be in the form of a memo from Michael to Mr. Wolfensohn. Kate will fax it to Michael for his approval. Thanks. Greg Ingram (We faxed a copy to Alan today.)			
FROM Gregory Ingram		ROOM NO. N9-033	EXTENSION 31052

OFFICE MEMORANDUM

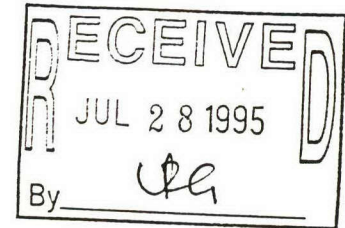
DATE: July 28, 1995

TO: Mr. James D. Wolfensohn, EXC

FROM: Michael Bruno, DECV *MB*

EXTENSION: 33774

SUBJECT: **Board Seminar on Relations with the WTO**



1. On July 26, the Board discussed possible modalities for cooperation between the Bank and WTO. The discussion was structured around the mandate which the WTO members had given their Secretariat to negotiate arrangements with the Bank. The staff had circulated an annotated version of this mandate setting out the background to the issues and the alternatives that might be open to the Bank in negotiations. The seminar went well and the discussion was generally supportive and constructive.

2. The Board expressed wholehearted support for cooperating with WTO and for concluding negotiations speedily. The Board concurred that, despite their slightly differing mandates, the Bank and WTO shared many common objectives and should seek to act in a mutually supportive fashion. They recognized that the Bank would frequently support countries in pursuing policies that were permitted but not required by the WTO and agreed that Bank and WTO advice should try to distinguish carefully between policy recommendations that were necessary to meet the requirements of WTO and those that were desirable in the name of good economic policy.

3. On specifics, there was a broad consensus that the Bank should seek observership on the WTO's Dispute Settlement Body, and that in return it should offer some form of observership at its own deliberations. The majority opinion was that the Director General or his representative should be invited to observe Board proceedings at all general discussions of international trade and trade policy, and that they might observe some country discussions when trade policy was a major component. Most Executive Directors felt that invitations to country discussions should be at Bank discretion, but that the WTO might solicit invitations on its own initiative. A few Executive Directors did not wish to go so far but there was little opposition to WTO attending general discussions. It was universally agreed that informal contacts at staff level were the best means of making cooperation and collaboration operational.

great 4. We will start discussions on cooperation with the WTO, and also with the IMF, with which we wish to maintain a degree of parallelism on this matter. When we are close to agreement we will consult with you and then draw up a draft memorandum of understanding for submission to the Executive Board and ultimately

the Board of Governors. I hope this will be in time for the WTO to approve the arrangements at their General Council meeting in November this year.

5. Two other contentious issues arose at the Board Seminar. First, Mrs. Herfkens and Mr. Gerber stressed the importance for the Bank to reopen its office in Geneva, arguing that only through full-time official representation, could the Bank adequately monitor and cooperate with activities in the WTO. We replied that we would review the future of the Geneva office as the form of cooperation with WTO emerged over the next year or so. They will probably come back to this issue at some stage.

6. Second, Executive Directors representing transition countries which are currently not members of the WTO complained that the Bank did too little to aid these countries' accession to WTO. We explained that the Bank gives a good deal of general advice on international trade policy to these countries but that, despite our strong desire that they should accede to the WTO, we were neither qualified nor institutionally able to become involved in the detailed negotiation of accession. Moreover, the WTO Secretariat already provides technical assistance on detailed negotiating issues. We explained that, subject to resource constraints, the Bank would entertain any requests for assistance that these countries' authorities made. Executive Directors, and particularly Mrs. Herfkens, were still unhappy with the extent of Bank support on trade issues for these countries. As a result, in consultation with the ECA Region, we are compiling an inventory of the Bank's recent trade-related work in these countries.

I wd like to see it

30760

c.c. Messrs. G. Kaji, S. Sandstrom, R. Frank, EXC,
M. Ahmed, L.A. Winters, J.M. Finger, IEC

Thank

hi

8/1

*Please
Ask
someone to
get me the
background
on this*

The World Bank
Washington, D.C. 20433
U.S.A.

Note
J.W. Chron

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

September 6, 1995

Mr. James D. Wolfensohn
EXC

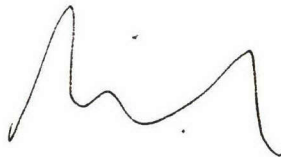
Dear Jim:

The attached note responds to the request you made at today's briefing. The points made deal with:

- (1) the importance of developing countries in the growth of US exports; and
- (2) the growing size of developing country markets

The table gives some supporting statistics in purchasing power parity dollars.

Sincerely



The Importance of the Developing World to US Exporters

- Almost half of the growth in US exports over the last 10 years went to developing countries.
- In 1993, developing countries took **twice** as much in US exports as the members of the European Union.
- During the recession of 1991-93, US exports to developing countries grew 5 times faster than exports to other industrial countries.
- During the last 10 years, US exports to developing countries in Asia have grown twice as fast as those to Europe.

Source: World Bank, Global Economic Prospects and the Developing Countries, 1995.

The Growing Importance of the Developing World in World Markets

- China is now the third largest economy in the world, after the US and Japan. By 2007 China will overtake the US as the largest economy in the world.
- High growth in the developing countries is not confined to China. By 2010 India will be the third largest and Indonesia will be the sixth largest economy in the world.
- 64% of the total increase in GDP of the world's 10 largest OECD and 10 largest developing economies between 1990 and 2010 will originate in the 10 largest developing economies.

Source: World Bank, Global Economic Prospects and the Developing Countries, 1995, and World Bank data.

Tables

GDP levels in 1993 International dollars (billions) *							
Years:	1980	1990	2000	2004	2010		
HIGH-INCOME OECD..							
United States..	4672	6072	7632	8416	9704		
Japan..	1640	2457	3198	3620	4347		
Germany (Unified)..	1049	1308	1677	1875	2213		
France..	854	1081	1323	1469	1713		
Italy..	808	1005	1209	1316	1491		
United Kingdom..	773	1006	1217	1342	1557		
Spain..	390	523	664	752	909		
Canada..	432	575	736	830	991		
Netherlands..	209	256	319	348	399		
Australia..	217	292	405	453	547		
LMIC TOTAL..							
Brazil..	692	804	1070	1249	1581		
China..	840	1949	5031	6986	11460		
Mexico..	485	572	742	869	1113		
Korea..	147	351	679	873	1274		
Russia	877	1181	749	904	1197		
Argentina..	244	222	347	397	485		
India..	576	1012	1555	1954	2772		
Turkey..	124	203	278	336	452		
Indonesia..	283	488	928	1193	1731		
Thailand..	136	290	625	852	1352		
* – Methodology uses 1993 GDP in PPP dollars (taken from WDR95) and applies real GDP growth forward and backward (taken from GEP95 baseline).							
Top ten OECD and developing countries ranked by 1993 GDP levels in current dollars.							



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Correspondents / Participants From: Michael Bruno To: James D. Wolfensohn, President		
Subject / Title Re: World Bank Office in Geneva		
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Withdrawn by Salma Berrada	Date April 29, 2025	

The World Bank/IFC/MIGA

F I C E M E M O R A N D U M

DATE: October 24, 1995 11:04am

TO: Michael Bruno

(MICHAEL BRUNO)

FROM: Nimrod Raphaeli, OPRPG

(NIMROD RAPHAELI)

EXT.: 84015

SUBJECT: **World Bank Office in Geneva**

While in New York last Sunday, October 22, Mr. Wolfensohn inquired about the Bank's representation in Geneva. I drew his attention to your memo to him of August 31, and your subsequent note of September 8.

My impression is that Mr. Wolfensohn is very keen about reopening the office in Geneva (if I were more daring I would say he has made up his mind to do so). WTO is the prime reason but he also wants liaison with the UN.

CC: SVEN SANDSTROM

(SVEN SANDSTROM @A1@WBWASH)

CC: Armeane Choksi

(ARMEANE CHOKSI)

CC: RACHEL LOMAX

(RACHEL LOMAX @A1@WBWASH)

CC: Myrna Alexander

(MYRNA ALEXANDER)

CC: Mark Baird

(MARK BAIRD)

file copy

The World Bank
Washington, D.C. 20433
U.S.A.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

August 14, 1995

Mr. James D. Wolfensohn

Ref. Federal Reserve Bank of Kansas City
Jackson Hole Symposium
"Budget Deficits and Debt: Issues and Options"

Mr. Wolfensohn,

Attached is a background brief for your participation in the closing panel of the symposium, on September 2, 1995. The brief draws on a large research program recently completed by DEC and published as, W. Easterly, C. Rodriguez and K. Schmidt-Hebbel, *Public Sector Deficits and Macroeconomic Performance*, Oxford University Press, 1994. This research is the product of studies of Argentina, Chile, Colombia, Cote d'Ivoire, Ghana, Morocco, Pakistan, and Zimbabwe.

Please let us know if you have any further questions. Thank you.

Vinod Thomas

Vinod Thomas
Acting Vice-President, DEC

Attachment

cc: Mr. Michael Bruno (o/r)

August 14, 1995

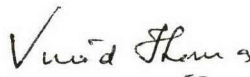
Mr. James D. Wolfensohn

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Please let us know if you have any further questions. Thank you.



Vinod Thomas
Acting Vice-President, DEC

Attachment

cc: Mr. Michael Bruno (o/r)

bcc: Messrs. Squire (o/r), Deverajan, Easterly, Schmidt-Hebbel, Serven, Vieira da Cunha

PUBLIC DEBT AND DEFICITS: LESSONS FOR DEVELOPING COUNTRIES

- **Large fiscal deficits are bad for growth and they increase poverty.**

Deficits are financed either by the domestic private sector (leading to high inflation and high real interest rates) or by foreign creditors (leading to large current account deficits and an appreciated real exchange rate). National saving is depressed and private investment suffers twice: It is crowded out by public spending and it falls in response to the instability that results from high inflation, exploding public debts, and unstable external financing. Economic growth falters. The poor are hit by high inflation that squeezes real incomes and money holdings, by the cut in public spending on basic services, and by the unemployment that results from economic stagnation.

- **Large fiscal deficits are not bad luck but bad policy.**

Temporary spells of bad luck, such as droughts, recessions or falling export prices, often hit public budgets adversely. But policy makers—not external circumstances—are to blame for persistently high deficits. They are also responsible for reducing and eliminating deficits. For example, 91% of the deficit reduction in Ghana after the onset of the *Economic Recovery Program* 1983 reflects tax hikes or expenditure cuts.

- **There are two stages for fiscal adjustment...**

The first stage of adjustment is to a sustainable deficit, defined as the level of public financing that is consistent with a stable debt-to-output ratio, low inflation, and liberalized markets for goods and financial assets. Estimations for many countries suggest that sustainable public deficits are in the range of 2% to 6% of GDP, with specific levels determined by each country's levels of public debt, real interest rate, inflation, and GDP growth. In the early 90s fiscal deficits

in Latin America fell from 6.6% to 2.1% of GDP.

To join the European Monetary Union, the Maastricht treaty imposes two specific fiscal conditions that have to be satisfied by each country before joining EMU: the government's budget deficit must not exceed 3% of GDP and outstanding public debt must be no more than 60% of GDP. (These two criteria are currently satisfied only by two—Germany and Luxembourg—of the 15 prospective members.)

The second stage of adjustment is to balance the budget or operate with a fiscal surplus. Some countries have already gone this far, including Chile, Korea, New Zealand, and Thailand. This second stage brings three additional benefits: greater credibility, greater saving and domestic investment, and greater flexibility of using fiscal policy as a cushion during recessions.

- **and two basic reforms: tax and expenditure reform.**

The *composition* of taxes and expenditures determines whether public policy inhibits or promotes growth and poverty reduction. Taxes on saving and investment affect incentives and impede growth; trade taxes protect inefficient domestic industries, drawing resources away from the export sector. Some 75 countries have lowered personal income and corporate tax rates, and sharply reduced trade taxes, in favor of a value added tax (VAT), which taxes consumption instead of savings and leaves exports untaxed. They have addressed the inequitable aspects of the VAT by lowering the rate on goods consumed by the poor. These countries have lowered distortions and achieved significant economic gains.

On the expenditure side, developing countries have made some progress during the 1980s in squeezing out white elephants, reducing military spending, and—although not widely recognized—protecting social spending. However, public spending in the social sectors continues to be

skewed away from high-return, pro-poor items such as primary education and preventive health care and towards university education and urban hospitals which the private sector can provide. Furthermore, outlays for crucial but politically less visible operations and maintenance (drugs, textbooks, road repair, etc.) have been reduced, even though these expenditures have been shown to yield extremely high rates of return (100 percent in the case of irrigation in Indonesia, for example).

- **Hidden deficits are ticking fiscal time bombs.**

Deficits and debts are often hidden in four public programs:

- pension systems;
- banking systems covered by guarantees on deposits;
- debts and deficits of state governments;
- public enterprises.

The implicit debt of *public pensions* is often larger than the explicit public debt. It stood at 128% of GDP in Chile in 1981 (the year of its pension reform) when explicit government debt was 30% of GDP. In Italy, a country that holds one of the highest ratios of debt-to-GDP in the world, the implicit pension debt exceeds 240% of GDP (as of 1990), twice the level of explicit government debt of more than 120% of GDP (in 1994). Chile has shown the way toward deep and successful pension reform by substituting its ineffective, public, pay-as-you-go pension scheme with a privately-managed, fully-funded pension system. Argentina, Colombia, and Peru have recently adopted similar reforms.

The *public insurance of banks* can be a costly liability. For example, Argentina's banking crisis of the early 1980s cost 55% of GDP. Mexico's current financial crisis may cost 10% of GDP or more in public bail-outs. The recurrent crises are often linked to sudden movements in interest and exchange rates. But they also reflect the adoption of incomplete financial reforms: liberalization without institution-building. Countries have liberalized interest rates, credit controls, and

international capital flows without upgrading sufficiently their prudential regulation and supervision, accounting and financial reporting standards, and legal systems. This policy gap, in conjunction with low bank capital and broad deposit insurance, provided the incentives for bank managers to bet the bank: "heads I win, tails the government loses".

A third fiscal obligation is the *public deficit of sub-national units of government* guaranteed by the federal authority. Though fiscal devolution can help raise the efficiency of expenditure and tax systems, a frequent risk of decentralization is that lower government levels do not face hard budget constraints. Fiscal decentralization in Brazil combined the transfer of half of central government tax revenues to states and municipalities and the use of credit issued by state-owned banks to finance state deficits. When added across all the states, this undermines monetary stability. When the state banks go bust, the states turn to the Central Bank for bail-outs.

Losses and debts of public enterprises are also a major fiscal liability. Low returns and dissatisfied customers and clients explain the world-wide trend of public enterprise restructuring and privatization. In defusing this fiscal time bomb radically through privatization, Latin America has shown the lead, with privatization proceeds topping \$ 55 billion during 1988-93. But privatization may be compromised by the use of revenues from divestiture to cover current spending. Instead, the capital should be used to build other public assets with higher returns or to pay-off public debt. Bolivia, for example, is linking state-enterprise privatization to pension reform, using part of its enterprise equity to pay off its implicit pension liabilities.

OFFICE MEMORANDUM

DATE: July 28, 1995

TO: Mr. James D. Wolfensohn, EXC

FROM: Michael Bruno, DECVP *MB*

EXTENSION: 33774

SUBJECT: **Board Seminar on Relations with the WTO**

1. On July 26, the Board discussed possible modalities for cooperation between the Bank and WTO. The discussion was structured around the mandate which the WTO members had given their Secretariat to negotiate arrangements with the Bank. The staff had circulated an annotated version of this mandate setting out the background to the issues and the alternatives that might be open to the Bank in negotiations. The seminar went well and the discussion was generally supportive and constructive.

2. The Board expressed wholehearted support for cooperating with WTO and for concluding negotiations speedily. The Board concurred that, despite their slightly differing mandates, the Bank and WTO shared many common objectives and should seek to act in a mutually supportive fashion. They recognized that the Bank would frequently support countries in pursuing policies that were permitted but not required by the WTO and agreed that Bank and WTO advice should try to distinguish carefully between policy recommendations that were necessary to meet the requirements of WTO and those that were desirable in the name of good economic policy.

3. On specifics, there was a broad consensus that the Bank should seek observership on the WTO's Dispute Settlement Body, and that in return it should offer some form of observership at its own deliberations. The majority opinion was that the Director General or his representative should be invited to observe Board proceedings at all general discussions of international trade and trade policy, and that they might observe some country discussions when trade policy was a major component. Most Executive Directors felt that invitations to country discussions should be at Bank discretion, but that the WTO might solicit invitations on its own initiative. A few Executive Directors did not wish to go so far but there was little opposition to WTO attending general discussions. It was universally agreed that informal contacts at staff level were the best means of making cooperation and collaboration operational.

4. We will start discussions on cooperation with the WTO, and also with the IMF, with which we wish to maintain a degree of parallelism on this matter. When we are close to agreement we will consult with you and then draw up a draft memorandum of understanding for submission to the Executive Board and ultimately

the Board of Governors. I hope this will be in time for the WTO to approve the arrangements at their General Council meeting in November this year.

5. Two other contentious issues arose at the Board Seminar. First, Mrs. Herfkens and Mr. Gerber stressed the importance for the Bank to reopen its office in Geneva, arguing that only through full-time official representation, could the Bank adequately monitor and cooperate with activities in the WTO. We replied that we would review the future of the Geneva office as the form of cooperation with WTO emerged over the next year or so. They will probably come back to this issue at some stage.

6. Second, Executive Directors representing transition countries which are currently not members of the WTO complained that the Bank did too little to aid these countries' accession to WTO. We explained that the Bank gives a good deal of general advice on international trade policy to these countries but that, despite our strong desire that they should accede to the WTO, we were neither qualified nor institutionally able to become involved in the detailed negotiation of accession. Moreover, the WTO Secretariat already provides technical assistance on detailed negotiating issues. We explained that, subject to resource constraints, the Bank would entertain any requests for assistance that these countries' authorities made. Executive Directors, and particularly Mrs. Herfkens, were still unhappy with the extent of Bank support on trade issues for these countries. As a result, in consultation with the ECA Region, we are compiling an inventory of the Bank's recent trade-related work in these countries.

c.c. Messrs. G. Kaji, S. Sandstrom, R. Frank, EXC,
M. Ahmed, L.A. Winters, J.M. Finger, IEC

The World Bank
Washington, D.C. 20433
U.S.A.

* Chron
J.W.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

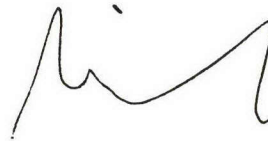
Mr. James D. Wolfensohn

July 12, 1995

Jim:

On July 25, you will chair a Board seminar on our Policy Research Report "Bureaucrats in Business: The Economics and Politics of Government Ownership." This report has raised several general issues such as the degree to which staff can examine political factors influencing economic outcome and the independence of research, both of which are summarized in the attached note. I have also attached the Overview to the report.

Several Part II EDs may request a meeting with you to discuss these issues before the Board seminar. I and my colleagues will be happy to brief you at your convenience. The issues being raised are important and warrant a considered response. You will already have received a legal opinion on these issues from Mr. Shihata.



cc: Mr. Gautam Kaji

Attachments

Issues raised under Other Business
at the Board meeting of June 22, 1995

This note addresses the issues raised by the Board regarding the Policy Research Report "*Bureaucrats in Business: the Economics and Politics of Government Ownership*." The Board raised three points, each of which in turn raises general concerns for the institution and specific ones for the report.

1. CLEARANCE PROCEDURES

The Board requested that we clarify the clearance procedures for different categories of Bank research products.

General. DEC research products take two forms usually aimed at different audiences. First, there is a variety of more technical products -- articles and books -- aimed at specific professional audiences. These are subject to internal and external review by professional peers. They do not go to the Board. Second, there are DEC Major Products that are agreed with and closely monitored by the Chief Economist. These reports are presented to the Board either for discussion or for information. Comments from the Board, received either bilaterally or at a Board discussion, have usually been handled in the following way. Factual inaccuracies are corrected but other comments are judged on their merit and incorporated at the discretion of staff. It is the responsibility of the Chief Economist to assure that Bank research reports are of the highest quality.

Specific. Policy Research Reports fall into the second category. In the specific case of *Bureaucrats in Business*, in addition to internal DEC reviews, the report was subject to a Bank-wide review and a PRC review. As agreed with the Steering Committee, a Board discussion of the report was not planned but it was sent to the Board with the understanding that a seminar could be held if required. (In the case of the previous report in this series -- *Averting the Old Age Crisis* -- the Board chose not to have a seminar.)

2. OPERATIONAL IMPLICATIONS

The Board requested that we clarify whether the note on Operational Implications recommended changes in Bank policy.

General. Policy Research Reports do not contain recommendations on Bank policies. But at Board discussions of these reports (and WDRs), the Board usually asks for a statement on implications for the Bank. To meet this need, our practice is to attach to the report sent to the Board a short note spelling out the implications for Operations. This note is not part of the published version of these reports.

Specific. The note on Lessons of Experience and Operational Implications accompanying the report does not propose changes in Bank policy. Rather, based on case study material and cross-country analysis, the note draws lessons from what has worked and what has not worked for policy implementation. It calls for a more cautious approach to public enterprise reform and a more thorough analysis of the pre-conditions for reform.

3. "POLITICAL ANALYSIS"

The Board questioned the analysis of Chapter 4 from two perspectives. First, whether such analysis was consistent with the Bank's Articles. And second, whether research staff had the capacity to undertake such analysis.

General. The analysis undertaken in Chapter 4 is consistent with the growing preoccupation of the economics profession with matters of political economy. Indeed, no analysis of policy can be considered complete without some assessment of when or in what form policy change is likely to be feasible and effective. *This type of analysis is especially important in the case of public enterprise reform where political factors often impede progress.* The analysis is also consistent with calls from several quarters, including OED, for more systematic analysis of government ownership, commitment, and readiness for reform. Finally, the analysis is consistent with the position taken by the General Counsel in his Legal Memorandum on Governance Issues, i.e., that the Bank cannot be influenced in its decisions by political factors but can take economic considerations into account even if they have political origins or are associated with political factors, as long as the economic effects are clearly established.

Specific. The analysis in the report is based on the following:

- In-depth country case studies by political scientists, sociologists and economists specialized in political economy and institutional economics.
- Assistance from political scientists (Mathew McCubbins and William Heller, University of California, San Diego) in the conceptual design and drafting.
- Extensive review of the literature and data and two years of analysis by three Bank researchers trained and published in political economy.
- Guidance from an outside panel of prominent experts, including Douglass North (1993 Nobel prize winner for his work on new institutional economics), Robert Bates (political scientist at Harvard University), John Waterbury (political scientist at Princeton University), Moises Naim (Carnegie Council), as well as economists such as: John Vickers (Oxford), Heba Handoussa (Economic Research Forum, Egypt), David Newbery (Cambridge), Oliver Williamson (Berkeley), and Vito Tanzi (IMF).

Bureaucrats in Business

The Economics and Politics of Government Ownership

(OVERVIEW)

Bureaucrats are still in business. Despite a growing consensus that governments perform less well than the private sector in a host of activities, and more than a decade of divestiture efforts in developing countries supported by the World Bank and other development institutions, state-owned enterprises (SOEs) account for nearly as large a share of economic activity in the developing world today as they did twenty years ago. Indeed, data compiled for this study show that the size of the state enterprise sector has significantly diminished only in the former socialist economies and a few middle income countries. In most developing countries, particularly the poorest, bureaucrats run as large a share of the economy as ever. Government employees operate a casino in Ghana; bake cookies in Egypt; assemble watches in India; mine salt in Mexico; make matches in Mali, and bottle cooking oil in Sénégal. More importantly, in many developing countries that continue to support large SOE sectors, the inefficiency of the state-owned firms, combined with the attendant state enterprise sector deficits, are hindering economic growth, making it more difficult for people to lift themselves out of poverty.

Consider these facts:

- In many developing countries, state-owned enterprises absorb large amounts of funds that could be better spent on basic social services. In Tanzania, central government subsidies to SOEs equal 72 percent of central government spending on education and 150% percent of central government spending on health.
- State-owned enterprises often capture a disproportionate share of credit, squeezing out private sector borrowing. In Bangladesh, state-owned enterprises take about one-fifth of domestic credit, although SOE output accounts for less than 3 percent of GDP.
- State-owned factories often pollute more than privately-owned factories. In Indonesia, government factories discharge about five times as much water pollution per unit of output as private factories of the same size and age engaged in the same activity.

- A modest improvement in state enterprise efficiency would substantially reduce and in some cases eliminate the fiscal deficit in most developing countries. In Egypt, Peru, Senegal, and Turkey, a mere five percent reduction in SOE operating costs would reduce the fiscal deficit by about a third.
- For these and other reasons, when state-owned enterprises account for 10 percent of GDP, about typical for a developing country, divesting just half can be expected to boost GDP by about 1 percentage point, with gains of similar absolute magnitude continuing year after year.

Many governments have announced plans to sell state enterprises and to improve the performance of firms that remain in government hands but only a few developing countries have made measurable progress. Our study found that:

- Developing countries excluding the transition economies are divesting an average of just three enterprises per year, although most governments own hundreds of firms.
- Non-divestiture reforms, such as hardening SOE budgets and instituting contracts between governments and the government-employed managers of state firms, have often failed to improve firm performance and have sometimes made things worse.
- While state-owned enterprise deficits have declined, they continue to be a significant burden to government finances and developing country banking systems.
- Notwithstanding the sale of some very large firms, the state enterprise share of developing market economies has remained stubbornly high since 1980, at about 11 percent of GDP, even as it fell in the industrial countries from about 9 percent to less than 7 percent.
- The state-owned enterprise sector is larger and the problems associated with it are more severe in the world's poorest countries, where SOEs account for 14 percent of GDP.

In sum, although the potential gains from privatization and other reforms are substantial only a few countries have reformed their state-owned enterprises successfully. Why haven't more

countries reformed their SOEs? What distinguishes the few that have from the many that have not? What are the political obstacles to reform, and how have these been overcome? How can leaders and policy makers in developing countries hasten reform and increase the likelihood of success? And finally, what can donor governments and multilateral institutions do to help? These are the questions this book sets out to answer.

To do so, we examine the economic problems that arise when bureaucrats are in business -- that is, when governments own and operate enterprises that could be run as private firms -- and the political obstacles to change. We do not suggest that bureaucrats are to blame for these ills. To the contrary, we find that divestiture and other state enterprise reforms cannot succeed without a sound bureaucracy. Requiring bureaucrats to oversee businesses better handled by private entrepreneurs places a heavy toll on developing country bureaucracies, diverting attention from problems that only governments can address. Bureaucrats typically perform poorly in business not because they are incompetent (they aren't) but because they face contradictory goals and perverse incentives that can distract and discourage even very able and dedicated public servants. The problem is not the people but the system, not bureaucrats *per se* but the situations they find themselves in as bureaucrats in business.

We begin our study by measuring the size and economic impact of the state-owned enterprise sector in developing countries. As noted above, we find that SOE sectors remain large in many developing countries, and that large SOE sectors have a negative effect on growth (chapter I). To understand the differences between the few countries that reformed successfully and the many that have not, we next investigate SOE reform efforts in twelve countries representing a broad cross section of regions and experiences. Our sample includes nine developing market economies (Chile, Egypt, India, Ghana, Republic of Korea, Mexico, the Philippines, Sénégal, and Turkey) and three transition economies (the Czech Republic, Poland and China). We find that countries that improved the performance of their state-owned enterprises made the most of divestiture, competition, hard budgets, and financial sector reforms. In addition, all twelve countries tried to improve the incentive structure by changing the relationship between government and state enterprises. The last measure rarely worked alone

(chapter II). To discover why, we go a level deeper and explore changes at the enterprise level. We find that improving the performance of SOEs or privatized monopolies requires a better incentive structure, that is, it requires rewriting the contract between government and SOE management, or between government and the owners of a privatized, regulated monopoly, so that both are motivated to improve performance (chapter III).

Taken together, this analysis shows that divestiture and other reforms can indeed improve SOE performance, but that only a few governments have adopted the policies necessary to reform successfully. Why haven't more governments attempted these policies? To answer this question, we investigated the politics of state-owned enterprise reform in our twelve country sample, identifying political obstacles and the ways that successful reformers overcame them (chapter IV). What can policy makers and the development community do to speed the reform process? Our final chapter draws on the findings of the previous work to construct a decision tree that reform advocates can use in deciding whether or not a country is ready for reform, and how to proceed in each instance. We conclude with a *Message to Donors* outlining steps that outsiders can take to encourage reform. The remainder of this Overview highlights the central arguments and findings of the book from chapter II onward.

What Makes for Success in State Enterprise Reform?

To understand the differences between successful and unsuccessful SOE reform, we first need an objective measure of success. We establish three objective indicators: state enterprise financial returns, state enterprise productivity, and the state enterprise savings-investment deficit (for a detailed discussion of these measures, see pp. XX-XX). Using these indicators, we find that Chile, Korea and Mexico achieved the best results; Egypt, Ghana and the Philippines had mixed results; while India, Sénégal and Turkey had the poorest results. Although we lacked comparable data for ranking the three transition economies, partial indicators suggest that the Czech Republic, Poland and China show mixed results.

What explains these differences? To find out, we considered the extent to which each country in our sample used five components of reform that economic theorists and reform

practitioners widely recommend -- divestiture, competition, hard budgets, financial sector reform, and changes in the institutional relationship between SOEs and government. *We found that the more successful reformers made the most of all five components.* Indeed, they used them not as separate options but as mutually supportive components of an overall strategy. Other countries in our sample achieved less in individual reform elements and followed a less comprehensive strategy overall.

Key findings about the ways that successful reformers, on one hand, and the mixed performers and least successful performers, on the other, approached each of these five components of SOE reform include the following:

- *Successful SOE reformers divested more, especially where the initial size of the state enterprise sector was more than 10 percent of GDP. (see pages XX - XX)*
- *Successful SOE reformers introduced more competition. They liberalized trade, eased restrictions on entry and unbundled large enterprises. (see pages XX - XX)*
- *Successful SOE reformers hardened SOE budgets. They reduced or eliminated direct subsidies, put access to credit on a more commercial basis, strengthened regulation of SOE monopoly prices and reduced or eliminated hidden subsidies. (see pages XX - XX)*
- *Successful SOE reformers reformed the financial sector. They strengthened supervision and regulation, relaxed controls over interest rates, and reduced directed credit. They also relaxed entry restrictions and privatized banks once SOE reform and supervisory and regulatory reform were well underway. (see pages XX - XX)*
- *Surprisingly, successful and unsuccessful reformers alike tried to improve the incentive structure by changing the relationship between SOE managers and the government.*

Countries at the top and bottom of our performance ratings introduced new oversight bodies, increased managerial autonomy and signed explicit performance agreements.

Why did the apparently similar efforts to change institutions produce different results? Partly, such institutional reforms only work in conjunction with the other reforms just described. In addition, there may be differences in the ways that countries designed and implemented these changes that would show up only at the micro level, in detailed firm level analysis. To find out, we analyzed the ways that governments rewrote their contracts with managers of state enterprises, with private managers contracted to run government firms, and with the owners of privatized, regulated monopolies.

Contracting: What Works, What Doesn't, and Why

Each relationship between a government and the manager of a state-owned enterprise, or between a government and the owner of a regulated, private monopoly, can be seen as a contract, that is, an agreement between the government and the other party based on shared expectations. Written contracts have been established for only a small proportion of the state enterprises world wide, but their use is growing. Countries often use written contracts for their most important and problematic activities, such as infrastructure monopolies (electricity, water, telecoms), and major exporters and revenue earners (tea in Sri Lanka, gold in Ghana, and hotels in Egypt). Yet little is known about whether such contracts work, what distinguishes the successful contracts, or which type of contract works best in which circumstances. Our study focused on three types of contracts:

- *performance contracts*, which define the relationship between government and a *government employee* managing a state-owned enterprise
- *management contracts*, which define the relationship between the government and a *private firm* contracted to manage a state-owned enterprise, and;
- *regulatory contracts*, the implicit or explicit contracts which define the relationship between the government and the owner of a private, regulated monopoly.

For each type of contract, we first examined a sample of firms to determine whether the contract improved performance; to understand differences in outcomes, we then analyzed how each contract resolved, or failed to resolve, problems in three areas: information, rewards and penalties, and commitment (for a brief description of these contracting problems, see pages XX - XX)

We found that performance contracts worked least well. Management contracts worked better, but only in circumstances identified below. Regulatory contracts, when properly designed and implemented, worked well for enterprises in monopoly markets. *Overall, then, the greater the participation of private agents in ownership and management, the better enterprise performance.* Our analysis suggests that this is because private managers and owners, unlike their government counterparts, could readily capture the benefits if performance improved; responding to these incentives, they worked harder than government managers and obtained better results. We summarize the main findings for each type of contract below.

Performance contracts rarely improve incentives, and may do more harm than good

Pioneered in France in the 1970s, performance contracts are currently used in twenty-eight developing countries. Our analysis of a sample of twelve companies in six countries gives little support to the premise that these contracts help improve SOE performance. Only three of the twelve case study companies showed a turnaround in total factor productivity (TFP) after contracts were introduced (Ghana Water, Mexico Electricity, and Sénégal Telecoms), six continued their past trends, while three performed substantially worse under contracts than before. The rates of return on assets deteriorated for three firms; the rest show little change.

Why did performance contracts work so badly? We found that these contracts were often mere formalities that did not improve, and in some cases exacerbated, the poor incentive structures facing government managers. Indeed, performance contracts failed to address all three contracting problems. They did not reduce the managers' information advantage; instead managers were able to use their knowledge of the firm to negotiate multiple soft targets that were easy for them to reach. Similarly, performance contracts rarely included rewards and penalties that could motivate managers and staff to exert more effort: where cash bonuses were offered they

had little effect because they were not linked to better performance; other promised incentives, such as greater managerial autonomy, were often not delivered; and penalties for poor performance, such as firing or demotion, were seldom applied. Finally, governments demonstrated little commitment to the terms of the contracts, frequently reneging on key promises. This increased managers' cynicism and their incentive to use their information advantage to negotiate soft targets.

Each of these problems can be seen with the performance contract governing Sénégal Electricity. The contract included twenty-two criteria for judging performance, but no rewards if managers attained them; moreover, government regulators lacked the power to reliably enforce penalties. Finally, while the government promised to take actions that would make it possible for the firm to meet its targets, such as forcing other state-owned enterprises to pay their electricity bills, these promises were often broken. Cynicism among firm managers has been high and the company has suffered declining productivity. Indeed, as with several other enterprises in our sample, it appears that the contract may have actually worsened incentives and performance.

Management contracts work, but only in some situations

Management contracts are not widely used, but were generally successful where they were attempted. Our worldwide search using a relatively broad definition (see page XX) found only 150 management contracts: forty-four involved hotels managed by major international chains; the rest were concentrated in agriculture and water. Our analysis of management contracts governing twenty firms in eleven countries found that profitability and productivity improved in two out of each three cases.

What were the characteristics of the successful management contracts? And, since they are often successful, why aren't they used more often? Analysis of the ways that the successful contracts addressed the problems of information, rewards and penalties, and commitment answers both questions.

Where management contracts succeeded, governments used competition to reduce management's information advantage. Of the thirteen successful contracts, ten involved SOEs in competitive markets, the other three involved competitive bidding for monopoly enterprises (two

water companies and a container port). Successful contracts also established meaningful rewards and penalties, usually by linking the contractor's fee to the firm's performance. Finally, successful contracts were set up in ways that elicited a strong commitment from both parties. For example, they were for longer periods with the possibility of renewal and provisions for arbitration of disputes. (See pages XX - XX)

Why aren't they more widely used? We concluded that the costs to the government of obtaining the information needed to negotiate, monitor and enforce a management contract are one reason that they are largely confined to hotels, agriculture and water. Information is more easily available, and contract transaction costs thus lower, in sectors where technology is not changing rapidly and output is single, homogenous product (as with water or sugar); or where the private contractor has an international reputation to protect, the market is competitive, and quality is easily compared (as with hotels). Moreover, under the conditions where management contracts can work, privatization will often provide governments with higher benefits (the selling price) and lower costs (no need to monitor, enforce and renegotiate the contract).

Regulatory contracts work, but require careful design.

Nearly all privatized firms providing infrastructure services operate in monopoly markets where government regulation is needed to prevent firms from abusing their market power. These regulations, and other divestiture provisions, constitute a regulatory contract, that is, an agreement between the government and the firm owners about how the firm would be rewarded and the conditions under which it should operate.

To evaluate these contracts, we analyzed the experience in the seven developing countries where the basic telephone network is privately owned and government regulated (Argentina, Chile, Jamaica, Malaysia, Mexico, the Philippines and Venezuela). We found that regulatory contracts improved performance in most cases; investment and labor productivity increased significantly in five countries, and the quality and quantity of service usually improved rapidly. Not all regulatory contracts are successful, however, as we can see from a comparison of their successful use in Chile and the problems encountered in the Philippines. (see pages XX - XX).

Again countries with successful contracts addressed all three contracting issues. In Chile, for example, the government reduced its information disadvantage by selling the franchise for local telephone service through competitive bidding, and by injecting other elements of competition into the contract wherever possible. Price regulations were designed to reward improved performance and penalize failure to improve. Finally, the Chilean government demonstrate its commitment to abide by the contract to investors in many ways; for example, the legislature passed laws defining procedures for arbitration and appeal of disputes.

The overall evidence from our sample suggests that divestiture of state enterprises in non-competitive markets, accompanied by appropriate regulation, usually does result in greater efficiency, expanded service, and overall improved welfare. But only a small proportion of the countries with large government monopolies in non-competitive sectors have attempted regulatory contracts. Indeed, as we have seen, despite the potentially large economic benefits of divestiture and other types of SOE reform, relatively few countries have made a systematic, determined attempt to reform their state-owned enterprises. To find out why, we studied the politics of state enterprise reform.

The Politics of Reforming State-Owned Enterprises

The reform of state-owned enterprises can cut to the heart of a government's support base, because reforms almost invariably involve eliminating jobs and cutting long established subsidies. Not surprisingly, politicians carefully weigh any change in SOE policies, preferring policies that help them remain in office over policies that undermine support and may cause them to be deposed. How have the countries that reformed successfully overcome the political obstacles to reform? What can other countries learn from their example to hasten the reform process? In considering these questions, we found that there are three necessary conditions for successful reform:

- Reform must be politically *desirable* to the leadership. Reform becomes desirable to the leadership when the political benefits outweigh the political costs. This usually happens with a change in regime or coalition shift in which those favoring the status quo lose power. It

may also happen when an economic crisis makes SOE subsidies so costly that reform becomes preferable to the status quo, despite opposition within the ruling coalition.

- Reform must be politically *feasible*. Leaders must have the means to overcome opposition to reform, either by compensating the losers, thus winning their support, or by compelling them to comply despite their losses.
- Promises central to state enterprise reform must be *credible*. Investors must believe that the government will not renationalize privatized firms; SOE employees and others who fear that they may lose out in reform must believe that the government will deliver on any promises of future compensation.

Chapter IV describes these conditions in detail, drawing on the twelve country case studies, and the rankings of successful and unsuccessful reformers we presented in chapter II. Here we illustrate each condition with brief examples, then present possible predictors of reform readiness.

Condition I: Political Desirability

Reforms become desirable to the leadership in two complementary ways. The first involves a change in government: either an outright regime shift (as from Allende to Pinochet in Chile in 1973) or a shift in the governing coalition (as from de la Madrid to Salinas in Mexico in 1988) changes the leadership's constituencies in such a way that those who might lose from SOE reform are no longer a significant part of the leadership's support base. The second involves an economic crisis (for example, a drop in GDP or a sharp fall in net foreign assistance) that makes it increasingly difficult for the government to continue subsidizing SOEs (as, for example, in Chile, Mexico and Ghana). The size of the economic crisis needed to make reform desirable depends on how much the leadership relies on the support of those who benefit from the status quo.

All the successful reformers in our sample met the political desirability test, while most of the countries with mixed or poor SOE performance in the 1980s did not. Even though most of

the latter group experienced either a significant regime shift or economic problems that could have created an opening for reform, the continued importance of the SOE sector in the government's support base meant reform did not become politically desirable. In Turkey, for example, a regime change in 1980 resulted in numerous economic reforms. However, these efforts stopped short of privatizing or otherwise reforming state enterprises because SOE employees were crucial to the new government's support base.

Condition II: Political Feasibility

Reform is politically feasible when the leadership can secure the approval and support of other government entities whose cooperation is critical to success -- legislatures, bureaucracies and the state or provincial governments that are responsible for formulating policy or carrying out the reform. In addition, the leadership must be able to overcome opposition to reform from potential losers, such as SOE employees, especially when these groups are organized, numerous and ready to engage in demonstrations, work stoppages in strategic industries, and other actions which might be costly to the government. The likelihood of opposition is greatest when the enterprise has many extra employees -- in some SOEs up to 90 percent of employees may not be needed. In such instances, workers, rightly worried that reform may lead to layoffs, have a strong incentive to resist.

In all successful reformers in our sample, the leadership controlled the policy making and implementation apparatus when reform began; moreover, in each country the leadership used a mixture of compensation and compulsion sufficient to overcome resistance outside normal political channels. In Chile, for example, the military government in the 1970s both revised labor laws to curb union powers and offered handsome severance pay to port employees who might otherwise have engaged in job actions which could have disrupted the economy. In the 1980s, the government distributed SOE shares to the public as part of the privatization program, providing special allotments for SOE employees.

Ghana, which we rank as partially meeting Condition Two, illustrates the difficulties that mixed and poor performers faced in overcoming opposition to reform. Throughout most of the

1980s and into the 1990s, the Rawlings government controlled policy making. In 1985, to overcome substantial resistance to SOE reform, the government tried a mix of compulsion and compensation. On one hand, it reduced the power of the state enterprise union, detaining labor leaders critical of the reform; on the other, it began to give fired state enterprise workers more generous severance payments. With the approach of elections in 1992, however, the government became increasingly reluctant to compel compliance with decisions about layoffs. Severance payments became so expensive that the government had to abandon efforts to cut SOE employment.

Condition III: Political Credibility

The third and final condition for successful state enterprise reform is government credibility. We identified three ways to judge a government's credibility. First, governments have a reputation for keeping promises; for example, because they announced and implemented overall economic reforms, or have not previously expropriated private firms. Second, they face domestic restraints on policy reversal, such as constitutional restrictions which make it hard to overturn legislation or widely distributed shares in privatized SOEs which can create a large, pro-reform constituency. Third, they submit to international restraints, such as trade treaties or loan covenants, which make it costly to reverse reforms. Some mechanisms are more powerful than others. A government with a solid reputation, or strong domestic restraints, may enjoy sufficient credibility whether or not it accedes to international treaties. The reverse is not true, however: international restraints are usually too weak to confer credibility where other conditions are absent.

Differences in credibility can be seen in a comparison of Chile and Egypt. The credibility of Chile's SOE reform promises rested largely on a strong reputation gained from implementing trade liberalization, fiscal restraint, deregulation and tax reform. In contrast, Egypt in the 1980s did not have a record of sustained economic reform, as reflected in its low confidence score with foreign investors. There were few domestic restraints to protect reforms from being overturned. And although Egypt signed GATT, it was bound only to the less restrictive provisions reserved

for lower income countries. Even if SOE reform had been politically desirable and politically feasible (it was not), Egypt would have not been able to meet the third and final requirement of successful reform: that reforms be credible.

Predicting Reform Readiness

Knowing how countries rank on political desirability, political feasibility and credibility, we can predict reform outcomes. Table 1 shows how countries in our sample ranked for each of the three necessary conditions according to objective measures. Countries that met all three conditions reformed successfully. Partial fulfillment of these conditions was usually associated with mixed performance, the product of reform oriented governments struggling to balance the competing demands of different groups of supporters. Finally, countries that did not meet all three conditions performed poorly. *This illustrates a key finding of our analysis: reform cannot succeed until countries fulfill each of the three readiness conditions.*

What Can be Done to Spur Reforms and Improve Outcomes?

The evidence makes it abundantly clear that reducing the role of bureaucrats in business and improving the performance of the remaining SOEs can bring a country substantial economic gains. Yet reform has been slow and seldom successful. We conclude our study by suggesting ways that leaders and policy makers in developing countries, as well as multilateral institutions and donor governments, can foster more rapid and successful state enterprise reform.

A Decision Tree for Reform of State-Owned Enterprises

State enterprise reform involves a multitude of choices, each with its own set of problems and opportunities. The choices made will inevitably vary from country to country; but to lead to successful outcomes, they must be made in a logical order. It might seem obvious, for example, that countries will not reform successfully until the leadership perceives reform as desirable. Yet, perhaps precisely because the economic gains of reform are substantial, well-intentioned outsiders, including the World Bank, have sometimes attempted to prod developing countries

Table 1 Predicting Reform Success

Country	Condition I Desirability	Condition II Feasibility	Condition III Credibility
Good SOE performance			
Chile	●	●	●
Korea	●	●	●
Mexico	●	●	◐
Mixed SOE performance			
Egypt	○	◐	○
Ghana	◐	◐	○
Philippines	◐	○	◐
Poor SOE performance			
India	○	◐	◐
Senegal	◐	◐	○
Turkey 1983-87	◐	●	◐
1987-92	○	○	◐
Transition economies			
China	◐	◐	◐
Czech Republic	◐	◐	◐
Poland	◐	◐	◐

- Fully meets the condition
 ◐ Partially meets the condition
 ○ Does not meet the condition

Condition I: Fully met if coalition change OR exogenous crisis AND PE reform losers outside government's support base; partially if either of the necessary conditions are met; not met otherwise.

Condition II: Fully met if reformers can secure approval AND design sufficient compensation packages to defuse opposition; partially met if one or the other is true; not met otherwise.

Condition III: Fully met if government known for keeping promises, faces domestic execution restraints on policy reversals and submits to international restraint on policy reversal. Note that by OECD standards, in which countries score much higher in ICRG (Switzerland with thirty, for example), and receive scores of seven on executive constraints, none of the sample countries would be judged to fully meet Condition III. For the purposes of this table, Chile, Korea and the Czech Republic were used as benchmarks against which the remaining countries in the sample were compared. In general, countries that did worse than these three countries in one dimension of credibility and no better than any others were judged to partially meet Condition III; countries that did worse on two dimensions and no better on others were judged not to meet the condition.

Source: See text.

that are not ready for reform into acting. Similarly, developing country leaders and policy makers, persuaded of the benefits of reforming state-owned enterprises, have sometimes attempted to do so only to choose an option that meets with failure. How can those who rightly favor reform organize the multitude of choices they face in a way that will increase the likelihood of success?

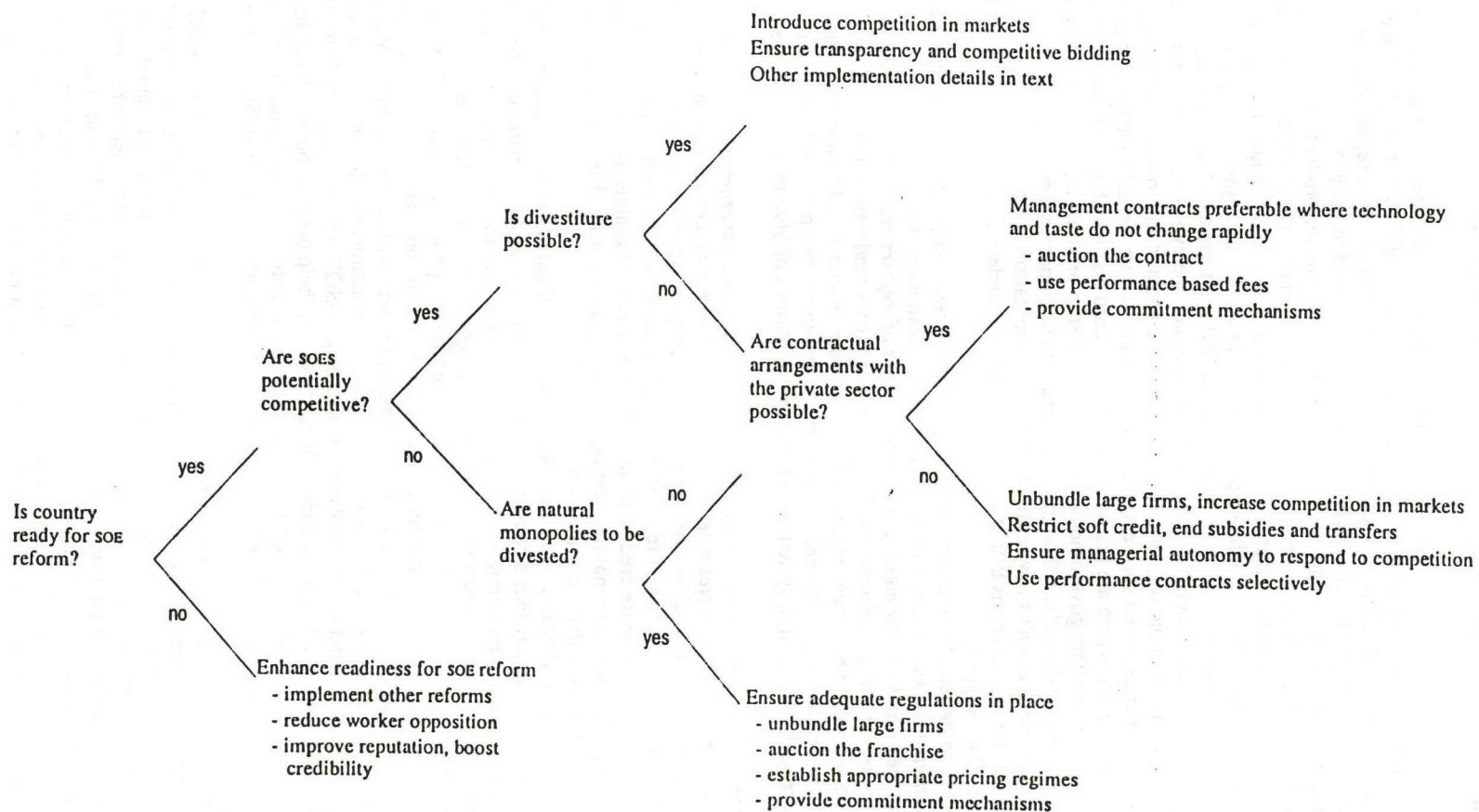
In thinking about the prerequisites of reform, and the conditions that are necessary for the success of various reform options, we have found it useful to draw a decision tree (figure 1). At each juncture we ask a question, the answer to which sends us in one of two directions, where we encounter another juncture and another question. Chapter V describes that decision tree, offering checklists that reform advocates can use in deciding how to proceed in a particular country or with a particular enterprise in order to avoid the potential pitfalls along the way. We conclude this overview with a brief summary of the main decision points.

The first question: is the country ready for reform or not? The answer will be determined by whether or not a country meets each of the three readiness conditions described above. In the borderline cases, of which there may be many, upfront actions, such as trimming an oversized SOE workforce or selling or liquidating a large firm, can be a good signal of readiness to proceed with a broader program of SOE reform. Depending on the answer, the course of action is radically different. *If the country is not ready, then SOE reforms should not be pursued*; even so, there are many other things that policy makers can do to lay the groundwork for reform. Because multilateral institutions and donor governments have been active advocates of SOE reform, and because their actions are an important influence on the timing of SOE reform and how it is pursued, we make recommendations for donors in *A Message to Donors* at the end of the book, summarized here in box 1.

What To Do in Countries Not Ready to Reform State-Owned Enterprises

Failed reform attempts can be very costly. Money spent to restructure state enterprises and pay off their bad debts is wasted if the enterprises fail to improve or, having been privatized, collapse. More difficult to quantify, but no less important, are the costs in wasted human and

Figure 1 A Decision Tree for State-Owned Enterprise Reform



Box 1 How Donors Can Better Assist State Enterprise Reform

The findings of this report, particularly the three conditions of reform readiness, have important implications for donor governments. External support for SOE reform is often highly beneficial, but the evidence suggests that it can do harm as well as good. This box summarizes the implications of the report's findings for donors; a more detailed discussion is presented in the Message to Donors at the end of the book.

We found that aid intended to promote SOE reform can be counter-productive in several situations. First, financial assistance to unready countries may make it easier for interests that oppose reform to sustain the status quo. For example, in at least two of our case study countries, Egypt and Sénégal, foreign assistance that ameliorated a fiscal crisis may have reduced pressure to reform. Second, going through the motions of reform without making real changes can cause a deterioration in SOE performance. For example, we found that signing a performance contract without changing incentives may heighten the cynicism of managers while giving them an opportunity to negotiate multiple soft targets at odds with the goals of improved performance. Third, we found that governments that ended overt state enterprise subsidies at donors' behest sometimes then expanded covert subsidies and bank credits, which are harder to identify and curb and which spread SOE problems to the financial system. Fourth, some reluctant governments dragged their feet in privatizing, then rushed into bad bargains to meet donor deadlines. And finally, although this is harder to document, support for reforms which are not implemented and therefore don't show results tarnishes the reputation of reform advocates in developing countries, and the donor institutions that attempt to assist them, undermining the credibility of SOE and other types of reform. This suggests:

- *Donors need to be selective and patient, following a different course of action in countries which are ready to reform their state enterprises successfully and those which are not.*
- *Only countries which clearly meet the three conditions of reform readiness should be encouraged and assisted in the pursuit of SOE reforms.* To gauge a country's readiness to reform, donors and multilateral institutions will need a better understanding of the constituencies that determine policies. Many donors already try to determine government commitment to recommended policy actions; our suggestion is to do this more reliably by focusing systematically on the conditions of SOE reform readiness that underlie success.
- *For borderline cases (which may well be the majority), up front government actions are the most reliable way to determine which countries meet the three conditions for successful reform; where commitment is uncertain, such actions should be a precondition for support.* Actions which signal that reform has become politically desirable and politically feasible include, for example, laying off extra workers or selling a very large firm; actions that increase credibility include establishing restraints to prevent policy reversal (such as constitutional prohibitions on renationalization) or widely distributing shares in privatized firms (thus creating a constituency with a stake in reform success).
- *Donors should also be alert to signals that they have overestimated reform readiness, or that circumstances have changed in such a way that a country no longer meets the readiness criteria.* These include moves to protect PEs from competition, writing off state enterprise debt without addressing the underlying causes of overindebtedness, or failing to pay state enterprises for goods or services delivered.
- *Donors should help governments of unready countries lay the groundwork for SOE reform by encouraging and assisting policy reform in other areas.* As we discuss in the text, this leaves a large agenda, including the reduction of fiscal deficits and trade restrictions, and removal of barriers to entry. While the similar tests of readiness may well apply to reforms in other areas, the constituencies for and against reform differ depending on the policy and sector involved; thus some non-SOE reforms are possible in countries where the conditions for SOE reform do not yet exist. Donors can also help prepare the way for SOE reform by providing information about the net costs of maintaining the status quo and the net benefits from reform, and by informing political leaders, policy makers, opinion leaders, and others about SOE reform experiences in other countries.
- *Donors can help reform ready governments attract private investors.* A government which is otherwise ready to reform but just beginning to establish its credibility may find it hard to attract private buyers for large, asset specific investments in regulated monopolies. In such instances, guarantees by international agencies could be investigated as a way to help attract initial private investment while the government is building up its credibility. Such guarantees are not without risk and should be approached cautiously, taking into account the pros and cons, which we discuss in box 5.1. Even without guarantees, donors and multilateral institutions can signal to investors which countries appear ready to reform their state enterprises by clearly distinguishing assistance to those that are ready from assistance to those that are not.

political capital. *Reform of state-owned enterprises should therefore not be attempted in countries which do not meet the three conditions of readiness.*

Are we suggesting that nothing can be done in such situations? Certainly not. Rather, policy makers can take actions which are beneficial in their own right, and also make state enterprise reform more desirable and feasible. Such reforms are often possible in environments where SOE reforms are not because they affect different constituencies. Macroeconomic reforms, for example, can increase the pressure and support for SOE reform, thus making it politically more desirable:

- *Reduce fiscal deficits.* Fiscal and monetary reforms that bring revenues and expenditures into line also increase pressure for SOE reform by making the burden of SOE deficits explicit.
- *Ease trade restrictions.* Liberalizing trade restrictions gives exporters a stronger position in the economy, and exporters can become an important constituency for SOE reform, demanding more efficient provision of goods and services that SOEs supply.
- *Remove barriers to entry.* Removing barriers to entry increases the number of voices calling for SOE reform. New entrants who must rely on state enterprise services or compete with subsidized SOE products help enlarge the constituency for reform.
- *Initiate financial sector reform.* Governments not ready to reform SOEs may still be prepared to develop their financial system by improving supervisory and regulatory capacity, reducing directed credit and direct government control over financial intermediaries, and easing some interest rate controls.

Similarly, governments can make SOE reform more feasible by reducing the opposition to reform by workers and others dependent on state enterprises. Actions include:

- *Eliminate obstacles to private job creation.* One reason state enterprise workers typically oppose reform is that while overstaffing makes layoffs likely, similarly appealing alternative employment is often lacking. Policy makers can thus ease the way for SOE reform by improving private employment opportunities. Steps include eliminating interest rate subsidies

(these encourage employers to substitute capital for labor) and complex employment regulations (which have been shown to inhibit private job growth).

- *Uncouple SOE jobs and social services.* State workers who receive many goods and social services through their jobs are especially fearful of being fired. In most transitional economies, for example, state firms traditionally provided housing, health care, transport, educational assistance and other benefits. Creating alternatives to enterprise benefits, such as a commercial housing market or public health care, enables SOEs to stop providing these services and offer offsetting higher pay instead. This gives workers greater mobility and reduces their resistance to reforms that may threaten their jobs.

Finally, governments can take actions to enhance their credibility:

- *Improve government's reputation.* By announcing reform programs such as the macro reforms mentioned above in advance and adhering to the program scrupulously governments can enhance their reputation with potential reform supporters.
- *Establish domestic and international constraints.* Enacting and adhering to constitutional provisions guaranteeing the right to property can help reassure investors that the government will honor its commitments. Trade treaties and multilateral agreements raise the cost of reversing future SOE reforms and help enhance credibility.

Policy makers that pursue this agenda will eventually find themselves on the opposite branch of the decision tree, among countries that are ready for SOE reform.

What to Do in Countries Ready to Reform State-Owned Enterprises

A country that meets the political conditions for successful SOE reform faces a multitude of choices about how to handle each enterprise, the answers to which will depend on the nature of the market, the firm, and the country's capacity to divest and, in the case of monopoly markets, to regulate. Returning to our decision tree, we see that it asks policy makers in countries ready to reform to classify SOEs into two types:

- Those operating in competitive or potentially competitive markets (all manufacturing and most services), and

- Those operating in natural monopoly markets where regulation is necessary to protect consumers (some utilities and most infrastructure).

Enterprises in competitive or potentially competitive markets should be divested, provided that competition is enhanced and arrangements for the sale can be made transparent and competitive, or at least open to the possibility of competitive bidding. Some enterprises in natural monopoly markets can also be divested, provided that the sale is transparent and open to competitive bidding *and* that a credible regulatory structure can be put in place. These two outcomes correspond to the two outermost branches of our decision tree.

For both types of enterprises, policy makers undertaking divestiture face many questions that have different answers depending on country conditions, and in some instances on the size and condition of the enterprise being sold. Questions that policy makers should consider when designing a divestiture strategy include:

- *Is it better to begin with small enterprises or big enterprises?* Selling big firms first produces bigger welfare gains: the bigger the firm, the bigger the benefits. It also signals that the government is serious about reform and, properly done, can create new pro-reform constituencies. On the other hand, starting with small firms and gaining experience before tackling the large firms makes sense if bureaucratic capacity is the limiting factor.
- *Should the government financially restructure firms before selling them?* While some financial restructuring may be necessary, new investments are seldom recovered in the sale price. Even so, government assumption of SOE debt is sometimes the only feasible way to unload a company whose debt exceeds the sales value of its assets.
- *Should the government layoff workers before selling an enterprise?* Countries as diverse as Argentina, Japan, Mexico, and Tunisia have sometimes had to fire state enterprise employees prior to privatization. This is sometimes necessary because investors will not buy a firm where acrimonious labor disputes seem likely. Moreover, governments are usually better able than private investors to alleviate adverse social impacts of mass layoffs. Severance pay can reduce the risks facing SOE workers. (These and other questions are discussed on pages XX - XX)

Selling monopolies is more complex than selling firms in competitive or potentially competitive markets. Even so, as long as the sale is competitive and transparent and a credible regulatory contract can be devised and implemented, divesting monopolies can produce major welfare gains. Policy makers who decide their country is ready to divest state-owned monopolies will want to incorporate the following findings in their divestiture plans:

- *Regulatory contracts work better when governments reduce the firm's information advantage through competition.* In addition to competitive bidding for the contract itself, post-sale competition can be increased by splitting competitive activities from natural monopolies and breaking national monopolies into regional monopolies. In markets that still remain monopolies, the government should require the winning bidder to meet specified targets or lose the concession.
- *Price regulation is more effective when it allows firms to retain some of the benefits of improved performance while passing part to consumers in the form of lower prices.* Basing prices on information from sources other than the firm can eliminate the firm's incentive to inflate costs. Revising prices infrequently gives firms an incentive to cut costs between adjustments.
- *Credible regulatory contracts lower costs to the consumer.* Governments that credibly commit to meeting their end of the regulatory contract can drive a harder bargain with investors. When the regulatory contract is based only on a presidential decree or lacks provisions for impartial adjudication of conflicts, investors demand higher returns or greater monopoly powers to compensate for higher risk. When such costs are very high, policy makers may wish to improve credibility before divesting. Alternatively, they may seek external guarantees. (see box 5.2).

Even in countries where the leadership is committed to rapid and extensive privatization, some SOEs are likely to remain in government hands for a long time, for political if not for economic reasons. What to do with these enterprises is the final question on the decision tree, it asks: are contractual arrangements with the private sector possible? Management contracts with

the private sector are the preferred course; however, as we have shown above, these are useful only in a limited number of circumstances where the enterprise's technology changes slowly and output is primarily a single homogenous product (such as water and sugar), or where quality is easily monitored (such as hotels). (Guidelines for designing a successful management contract are discussed on pages XX-XX).

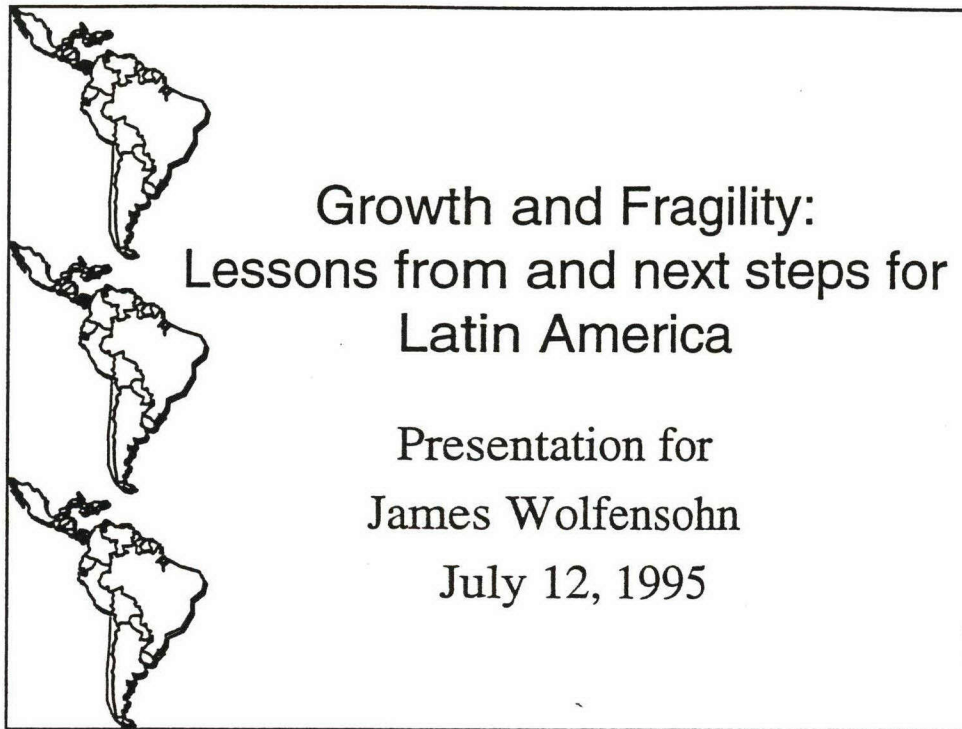
For firms that cannot be divested, but are unsuitable for management contracts, policy makers have no choice but to attempt improvements within the existing ownership and management arrangements. Specific measures that must be implemented include introducing competition, cutting government subsidies, reforming financial arrangements to eliminate soft credits, and holding managers responsible for results while giving them the freedom to make necessary changes. The performance of SOEs which are not divested can be improved through these actions, but getting the details right is tough because each reform relies on successful implementation of others. Policy makers should keep in mind the following:

- *Foster competition wherever possible to create incentives for improved performance.* State enterprise managers will only exert the effort needed to improve performance unless pushed by competition.
- *End subsidies and transfers.* Fostering competition is fundamental to improving the performance of SOEs in potentially competitive markets. But competition can only be effective if government transfers and subsidies are eliminated.
- *Eliminate access to soft credit.* Cutting subsidies and transfers only results in hard budgets if access to soft credit is also eliminated.
- *Give managers the autonomy to respond to competition and hold them accountable for results.* Managers must have the power to lay off workers, seek lower cost suppliers, end unprofitable activities and pursue new markets. And they must be held accountable for results. Lacking autonomy and responsibility, managers may respond to the increasing number of constraints in ways that hurt the enterprise, such as cutting spending on maintenance, marketing, even supplies.

- *Only use performance contracts when they address underlying problems.* Performance contracts should not be used unless they convey clear signals for reform, provide rewards for improved performance and curb governments' tendency to renege. Writing a sound performance contract can seem simple; as we have seen, however, they usually fail to address the problems of information, rewards and penalties, and commitment. In general, the effort that goes into such contracts would be better spent pursuing the measures described above, in particular putting in place the conditions for divestiture.

* * * *

In sum, we have shown that large and inefficient state enterprise sectors are costing developing economies dearly, especially the poorest among them. Yet reform is possible and offers potentially large benefits including more goods and services of better quality at lower prices; increased availability of resources for health, education and other social spending; and improved fiscal stability, all of which contribute to more rapid economic growth. Reforming state-owned enterprises isn't easy, however, and reforms often entail political costs. Indeed, we found that political obstacles are the main reason that state enterprise reform has made so little headway in the last decade. We hope that the research presented in this book will give political leaders, policy makers, and the broader development community a clearer picture of the substantial benefits that could result from state enterprise reform and, just as importantly, a better understanding of how the obstacles to reform can be overcome.



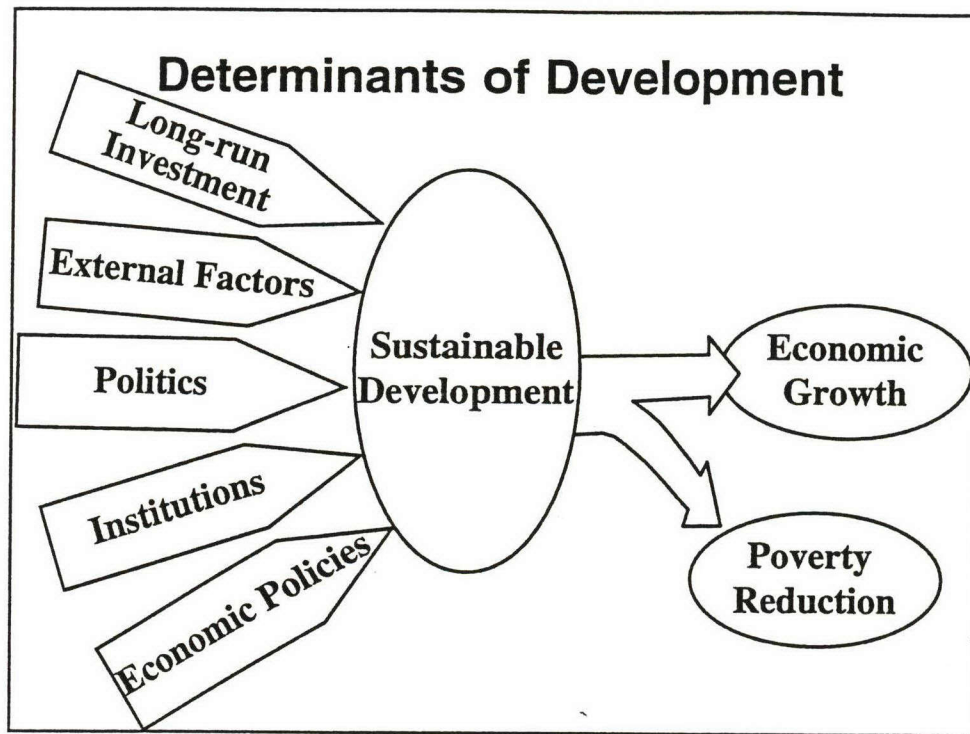
For much of this century and for many of its countries, Latin America has not been able to burst free from the political shackles that have restrained it from achieving and maintaining rapid economic development. The 1990s, however, saw the end of the debt crisis and hopeful signs of recovery.

Many of these positive signs owe themselves to a political transformation: populism has retreated and a more market-oriented agenda has taken its place.

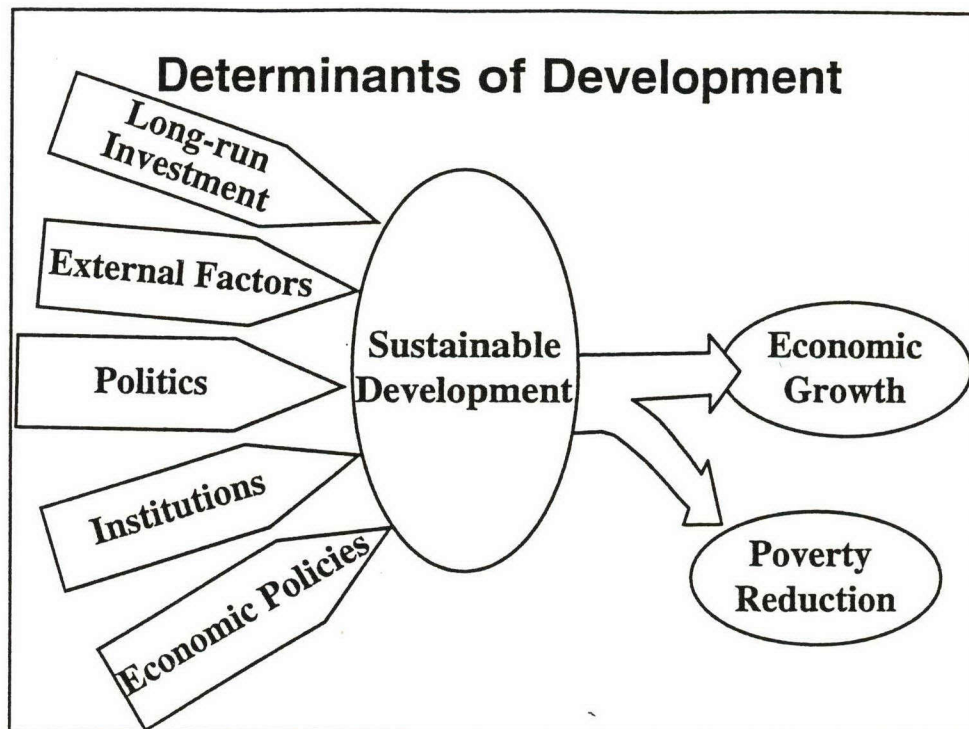
The calm optimism that spread with market reforms over the last few years was shattered, however, by the Mexican crisis.

International capital markets reared-up and asked: would Mexico and the rest of Latin America broaden and deepen economic reforms and thereby secure a sustained path of economic growth, or would they falter.

This morning we will discuss some steps Latin America can take to shake off these doubts about the fragility of economic reform and achieve faster rates of economic development

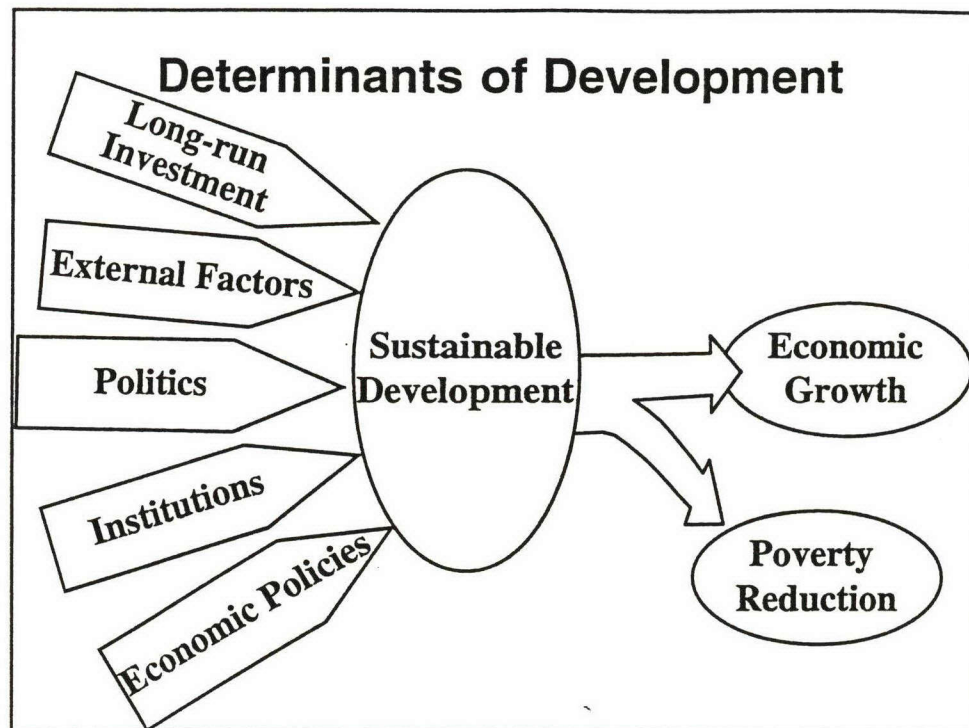


As you may recall from the presentation on adjustment and growth in Sub-Saharan Africa last month, economic development is a complex process with numerous determinants.

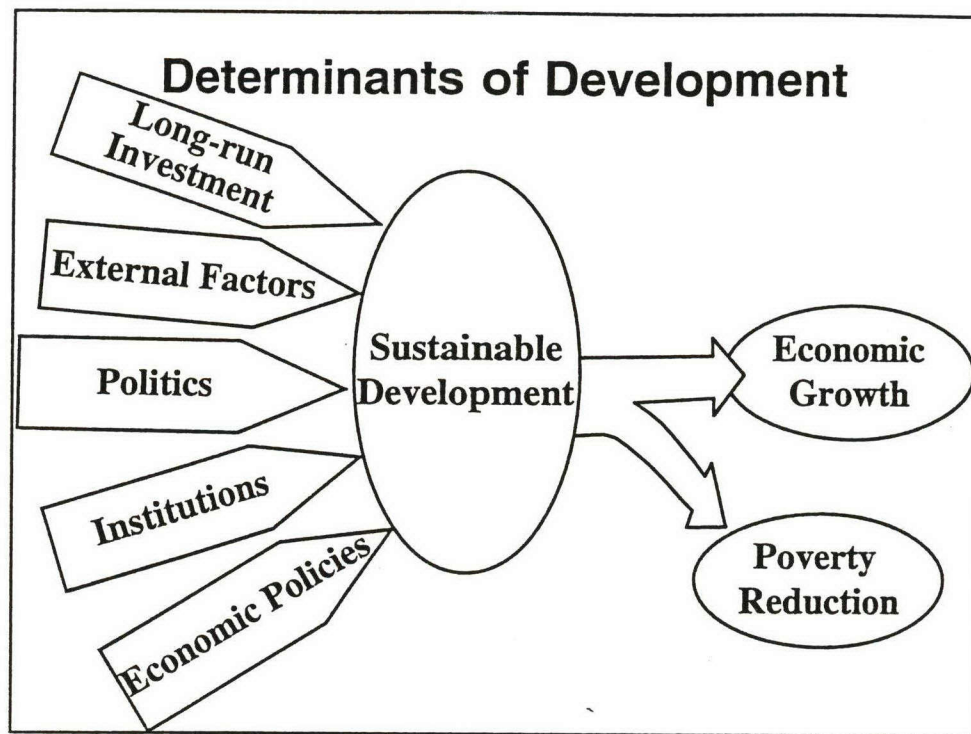


In the presentation on Africa, we focused on the role that economic policies play in affecting economic growth and through growth reductions in poverty.

Today, we broaden and deepen this analysis because most of Latin America is at a different stage of economic development from Sub-Saharan Africa.

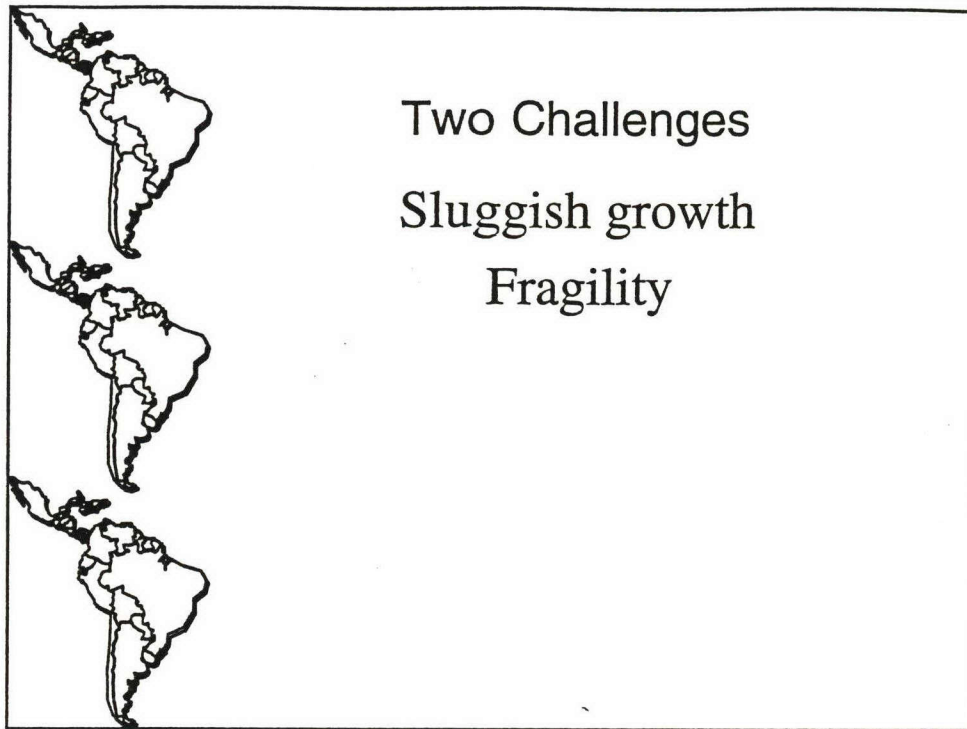


We broaden the discussion to include the role of external factors -- especially international capital flows -- and, we broaden the discussion to include the role of institutions -- especially the role of supervisory and regulatory institutions.

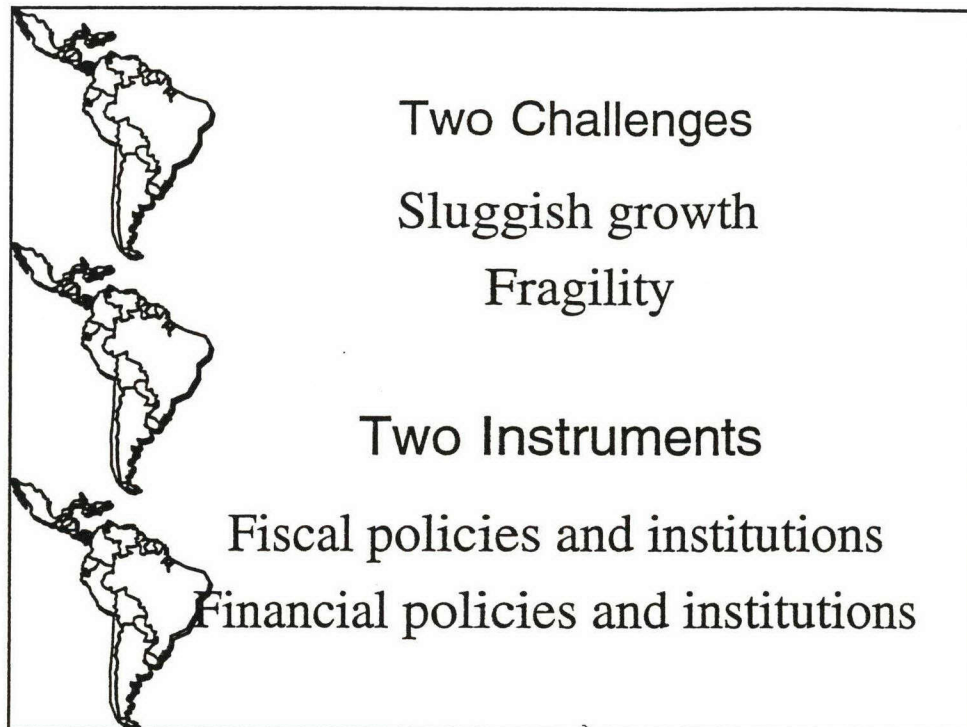


We will also deepen the analysis. Unlike Sub-Saharan Africa, Latin America is, with exceptions, at a second generation of policy reform. Fiscal deficits have been lowered, inflation has recently abated, and trade barriers are lower.

These first generation reforms are not enough; Latin American governments must deepen these initial reforms and establish a broad foundation for sustained growth during the 21st century.



Latin America faces a number of challenges. The Latin American region recently briefed you on issues of income inequality, poverty and political changes. Today we focus on two additional challenges facing Latin America -- sluggish long-run growth and a fragile recovery.



We examine two instruments for meeting the challenges.

We will first examine fiscal reform. Although deficits have been lowered, hidden government liabilities, or off-balance sheet items, like pension obligations and insurance of bank deposits, are growing. These growing fiscal obligations will eventually thwart development. Thus Latin America faces second generation fiscal reforms.

We also focus on the financial sector. Here too, much of Latin America is facing a second stage of policy reform involving the building of supervisory and regulatory institutions.



Topics:

- 1 Performance in Latin America and the Caribbean
- 2 Policy and institutional reforms to promote stability and long-run growth
- 3 What should the Bank do?

The remainder of the presentation this morning is divided into three segments. We first review the region's performance, focusing on Latin America's growth performance, its positive though fragile reform record, and its history with volatile foreign capital flows.

We then review fiscal and financial reforms to promote stability and growth.

Finally, we discuss changes in the World Bank that will give us a bigger development impact.

[Before continuing let me emphasize an important caveat. In this presentation, we often refer to "Latin America" as if it were a homogenous region. It is not. We make this generalizations to characterize much but certainly not all of Latin America and to highlight the policy, institutional, and external factors confronting many middle-income countries around the globe.]

The World Bank
Washington, D.C. 20433
U.S.A.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

Mr. James D. Wolfensohn

July 7, 1995

Jim:

DEC Follow Up of Presentation on Africa

This note responds to your request for ideas on how to use the DEC presentation on Africa in other venues. It also suggests some other follow-up actions flowing from the presentation. The points are summarized below and elaborated in the attached, one-page notes.

Presentation. The key point to emerge from the presentation is that aid to Africa has not been as effective as we would like. In the discussion, it was recognized that this in turn reflects, not a failure of staff, but a failure of the system -- the institutional incentives governing behavior account for the observed outcome. A presentation for staff could make this point and suggest changes, some of which are elaborated below. A presentation to external audiences -- the Annual Meetings, for example -- could stress the need for greater effectiveness against the background of past disappointments and the likelihood of lower aid volumes in the future. (See Note 1.)

Other follow-up actions. The presentation also highlighted two issues that merit your attention:

- i) the role of internal incentives in determining the observed outcomes (Note 2); and
- ii) the key questions to raise when reviewing Country Assistance Strategies (Note 3).

The first of these two notes illustrates what I believe is the key internal issue confronting the institution -- the role of incentives. Further reorganization and improved business practices are fine, but real change will require a change in incentives. The second one sets out actions you can take now during CAS reviews. If you consistently raise the key questions, staff will respond quickly.

I will, of course, be happy to discuss these suggestions with you in more detail if you so wish.



cc: Messrs/Mme. Richard Frank, Gautam Kaji (3), Sven Sandstrom, Atsuko Horiguchi

Attachments

NOTE 1
PRESENTATION POINTS ON AID AND/OR AFRICA

Internal Audiences

1. *The fundamentals matter.* It would be useful to convey to staff the importance you attach to getting the fundamentals right -- establishing the proper policy framework especially on the exchange rate and fiscal policy, and ensuring that adequate public resources are allocated to health, education, and infrastructure. The focus of our efforts must be on the basics if we want to reduce poverty. Staff know this. But it would be important for them to hear it from you, and to hear it consistently. To illustrate the importance of the fundamentals, the single most telling slide is the one which shows the growth "gap" between East Asia and Africa and the factors -- policy and investment -- that account for it.
2. *Our past record is not acceptable.* This is a tough message but should be delivered. The evidence is a decline in African GDP at the same time as we see large increases in aid to Africa (can be shown graphically). In our own case, the record shows too much money being lent to "adjusting" countries in Africa with little return in terms of better policies (can also be shown graphically). We have also failed to achieve significant improvement in the quality of public expenditures.
3. *The fault lies with the system, not with staff.* Having delivered the tough message on performance, it would be useful to establish that the problem lies with the system and not with staff. Staff are dedicated to development but the structure of incentives emphasizes volume of lending rather than development impact.
4. *Changing incentives.* This is a key issue and will require careful thought. The following examples illustrate the kind of changes that are required: budgets should be given to programs that get development results, not to ones that move loans; quality control has to be independent of Operations; promotion and compensation should be linked to quality of results, not quantity of loans. (See Note 2.)

External Audiences

The same general message can be used for external audiences but could be cast in the context of dwindling aid volumes and therefore the need to focus resources on countries committed to the basics. This is a two-edged message: countries must commit to the basics to receive money; and money must be made available to countries committed to the basics.

NOTE 2 INCENTIVES

The WB has invested considerable time and effort in reorganizations and in improving business practices and procedures. These are important and have their place. But the institution has paid less attention to the structure of incentives governing the behavior of managers and staff alike. And yet, it is these incentives that ultimately determine how well an institution performs. This note illustrates the general point with the specific (and important) example of the *quality* of lending.

1. *Observation.* As highlighted in the Wapenhans Report, about 40 percent of Bank projects are rated as "unsatisfactory" at the time of completion. This does not mean that these projects have failed. But it does mean that their development impact has fallen well short of expectations. Why?

2. *Reason One.* Incentives focus attention on the *volume* of lending, not the *quality* of loans.

- budgets are linked to lending volumes both at the level of the institution and that of the operating departments.
- recognition, promotions, and salary increases emphasize lending for new operations over the quality of the operation, over supervision, and over economic and sector work.
- performance contracts between different levels of management are couched in terms of number of projects to be delivered.

3. *Reason Two.* The emphasis on volume would not be an issue if the WB had a strong, independent mechanism of quality control. It does not.

- pre-Board quality control rests with the Regions, the producers of the loans.
- post-Board quality control lies with OED but occurs so late after appraisal that it is virtually impossible to identify and hold accountable the responsible staff.

Together, the two reasons are an important part of the explanation for the outcome noted above. The solution lies in changing the incentives -- breaking the link between budgets, performance contracts, and promotions on the one hand and lending volume on the other; and instituting an effective and independent mechanism of selective quality control. The Working Group on Non-Lending Services has developed specific proposals on some of these issues. Its report will be presented to you in the near future.

NOTE 3
MAKING BETTER USE OF THE CAS

The Country Assistance Strategy (CAS) is now the primary document for setting out the Bank's strategy in a country. However, despite some recent improvements, CASs are still very uneven in coverage and quality, and are generally poorly linked to management and budget decisions. One often comes away with the sense that nothing much has changed as a result of the CAS; it simply rationalizes what was already planned, and the actual program may well turn out to be quite different from the plan!

We believe you can reinforce the CAS and strengthen its strategic value by asking five basic questions:

1. *Is the Government committed?* This is the basic question which drives so much of the Bank's response. Without commitment, lending is likely to be wasted.
2. *What are the pressing policy and public expenditure issues?* This determines where the Bank should focus its analytical and advisory work. Without progress on these issues, Bank-financed projects are unlikely to succeed.
3. *What services can the Bank Group provide to help?* The CAS should lay out the full range of Bank services, including finance, analysis and advice. Non-conventional services -- workshops for private investors and policy seminars for parliamentarians -- should also be covered. The role and contributions of IFC and MIGA should be fully integrated into the strategy (e.g., for private sector development).
4. *What are our services expected to deliver?* We need to identify monitorable actions and performance indicators which signal our objectives and provide clear feedback on whether we are having the desired impact.
5. *What are our services expected to cost?* We rarely ask this question in the CAS. However, it is important to assess the efficiency of the proposed country program and to ensure that resources are being allocated to those countries who are committed to sound policies and will use our resources well. The CAS' decisions -- and follow up on impact -- should be reflected in budget allocations.

The attached matrix provides a simple and readable way to capture the main objectives and components of a country program, and to help answer some of these basic questions. We recommend that it be attached to the cover note for management review, with a simplified version (possibly excluding the monitorable actions and costs) included in the CAS itself. It can also provide a "living" summary of the country program to guide management and budget decisions between CAS reviews.

Illustrative Framework for Country Program

COUNTRY OBJECTIVES	MONITORABLE ACTIONS AND PERFORMANCE INDICATORS	BANK SERVICES / ^a	TASKS	BUDGET COSTS / ^b (US\$'000)		
				FY95	FY96	FY97
Maintain macroeconomic stability	Implement agreed fiscal envelope Finance BOP and budget gaps	Policy advice Import support Aid coordination	Fiscal policy note Structural adjustment loan Consultative group	50 20 -	- 40 40	- - -
Improve public sector management	Privatize 10 large loss-making PEs Change power tariff structure	Policy advice Networking	Structural adjustment loan Power sector seminar	20 -	40 -	- 40
Develop the private sector	Rehabilitate 100 km of rural roads Develop long-term bond market	Project financing Guarantee	Rural roads project Capital market guarantee	- -	20 -	80 50
Develop human resources	Reallocate public spending to basic health and education programs Refocus primary education program on classroom supplies and teacher training	Policy advice Policy advice Aid coordination	Public expenditure review Structural adjustment loan Consultative group	60 10 50	60 20 -	- - 50
Strengthen environmental management	Revise environmental law Establish pollution monitoring unit	Policy advice Technical assistance	Environmental management study Environmental TA project	50 -	- 50	- 30
		Country strategy	Creditworthiness study Public expenditure review Country assistance strategy	20 20 20	- 20 -	20 - 20
		Management & overheads	Miscellaneous	60	50	50
			Total	380	340	340

- a. For simplicity, stages of the project cycle (e.g., approval, supervision) are not shown separately.
- b. Includes all costs financed from the administrative budget and trust funds (services funded from client fees should be shown separately). For tasks serving more than one objective, costs have been allocated according to their relative importance.

NOTE 2 INCENTIVES

The WB has invested considerable time and effort in reorganizations and in improving business practices and procedures. These are important and have their place. But the institution has paid less attention to the structure of incentives governing the behavior of managers and staff alike. And yet, it is these incentives that ultimately determine how well an institution performs. This note illustrates the general point with the specific (and important) example of the *quality* of lending.

1. *Observation.* ~~In 1991 the Wapenhans report found that 40 percent of projects were judged unsatisfactory at the time of completion. Why?~~

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As highlighted in the Wapenhans Report, ^{we rated} OED ~~notes~~ about 40% of Bank projects as "unsatisfactory" at time of completion. This does not necessarily mean that these projects have failed. But it does mean that their development impact has fallen well short of expectations. Why?

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

July 5, 1995

Mr. James Wolfensohn

Briefing on the 1995 WDR for your visit to Europe

Jim,

Attached is a brief prepared by Michael Walton who, as you know, directed the 1995 WDR. I agree with his views and support his recommendations for future actions. We have prepared a note on operational recommendations emerging from the WDR. After approval by the Policy Review Committee, this note will be circulated to the Board and to staff. It is not, however, a public note nor does it change in any fundamental way existing Bank policy. I attach it for your information.

Thank you. I hope you have a good trip.



Michael Bruno

Attachments.

cc: Messrs. Walton, Baird, Vieira da Cunha (w/o att.)

The 1995 WDR: *Workers in an Integrating World*

This is to complement EXT's summary of press reaction to the WDR.

- *Seeking outside views.* In the preparation of the WDR we worked hard on interactions with union groups and the ILO. We also had a round of consultations with official agencies (bilateral, UNDP, UNICEF etc.) and a number of NGOs (including OXFAM, the Anti-Slavery society and several others). We met with Jerome Levinson of the 50 Years is Enough group. It is unclear whether they ever wanted a productive exchange. Two observations: they have an inordinate sense of the Bank's power in countries; they want something like a world policeman, that uses various forms of financial sanctions to protect what they think is worth protecting.
- *The ILO.* M. Hansenne was initially mad that the Bank was doing a big report on labor, in part for fear of competition with the ILO's World Employment Report but, thanks to Katherine Hagen (Deputy Director General), a reasonable understanding was reached and we received full cooperation in preparing the WDR. On substance, there are wide areas of agreement, but the ILO would still put greater reliance than us on legislative action to protect workers. They are wishy-washy on linkage between international trade and labor rights, reflecting strong differences of view in their governing council between the worker and employer groups, and within the government group. ILO's role is unclear, notably in the post-Cold War world.
- *Unions.* Interactions with union groups (via the international confederations, but involving representatives from many national unions) were productive throughout. We sometimes faced real anger, that seemed to flow in part from a feeling of being left out of the debate in the past. But they were highly responsive to our openness and offered constructive criticism. Differences remain, and in particular the unions are strongly committed to linkage of labor standards with international trade.
- *Other moderate critics.* Many who judged the Bank a heartless pusher of market philosophy (agencies such as UNICEF and UNDP, some of the Nordic development agencies, NGOs such as OXFAM, Christian Aid) appear to be cautiously welcoming the approach taken in the WDR.

Looking forward.

In terms of what the Bank can do differently in the future, I would emphasize three things:

- Continue to make progress on interactions with unions. However, the Bank faces genuine difficulties on what it can do in countries that restrict union rights, or where unions are highly politicized. This is a rather common feature in developing countries.
- Reach out with public programs to rural and informal sector workers (where we are already active), for whom direct government efforts are likely to pay off where legislation won't.
- Push more to reduce exploitative forms of child labor, since some of the instruments needed to tackle it are in areas of expansion of education and targeting of poverty measures where we have experience; the evidence indicates that NGOs or other civic groups are also key in this domain.

J.W. Chron

ROUTING SLIP		Date
NAME		ROOM NO.
Messrs. Ahmed		S8 055
Baird		
Squire		N11 051
URGENT	For Action/Comment	Per Your Request
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Approval/Clearance	Note And Return	See My E-Mail
File	Per Our Conversation	Signature/Initial
RE:		
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You may like to share this with your staff. Thanks Michael		
From	Room No.	Ext.
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The World Bank
Washington, D.C. 20433
U.S.A.

JAMES D. WOLFENSOHN
President

June 15, 1995

Mr. Michael Bruno

I would like to thank you and your colleagues for the admirable presentation on Africa. It was an outstanding piece of work, and I look forward to the next five presentations.

James D. Wolfensohn

A handwritten signature in black ink, appearing to read "James D. Wolfensohn", with a long horizontal flourish extending to the right.

THE WORLD BANK
Washington, D.C. 20433
U.S.A.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

June 15, 1995

Mr. James D. Wolfensohn,

Jim,

World Development Report 1995

I enclose a copy of the pre-publication copy of the WDR on labor. It will be released on June 30th.



Michael Bruno

THE WORLD BANK
Washington, D.C. 20433
U.S.A.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

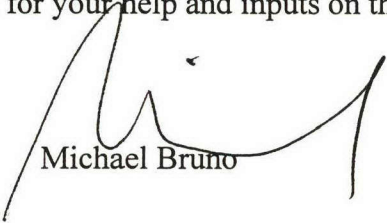
June 15, 1995

Mr. Gautam Kaji,

Gautam,

World Development Report 1995

I enclose a copy of the pre-publication copy of the WDR on labor. It will be released on June 30th. Thank you for your help and inputs on this project.



Michael Bruno

The World Bank
Washington, D.C. 20433
U.S.A.

Chris

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

Mr. James D. Wolfensohn

June 12, 1995

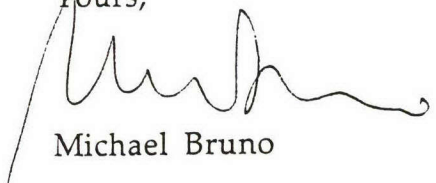
Dear Jim,

At the recent DEC meeting on development experiences you asked about The Economic Development Institute (EDI). I attach, for your information, a paper that describes the institute's newly emerging strategy.

You are scheduled to visit EDI on September 20 which will give you a first-hand flavor of the kinds of activities the institute carries out. At that time you will also be able to exchange views on EDI's new directions.

The changes under way should help EDI be a much more vigorous learning institution where country participants can learn about what has and has not worked. I have participated in an EDI seminar on macroeconomic reform for parliamentarians in South Africa and, as you suggested, we should and will be doing many more activities of this kind.

Yours,



Michael Bruno

The World Bank
Washington, D.C. 20433
U.S.A.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

Mr. James D. Wolfensohn

June 12, 1995

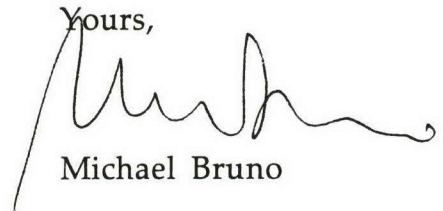
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Yours,

A handwritten signature in dark ink, appearing to read 'Michael Bruno', with a long, sweeping horizontal line extending to the right.

Michael Bruno

The Relaunching of EDI

THE ECONOMIC DEVELOPMENT INSTITUTE
DEVELOPMENT ECONOMICS * WORLD BANK

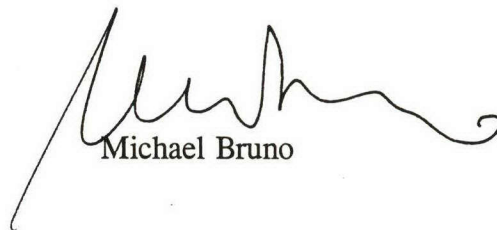
Mr. Timothy Thahane

June 13, 1995

EDI Strategy

Timothy,

Following your conversation with Vinod Thomas, I am attaching a status report on EDI's strategy for the information of the Board members.



Michael Bruno

Chen

The World Bank

1818 H Street, N.W.
Washington, D.C. 20433, U.S.A.

June 8 1995



With the compliments of

Michael Bruno

Vice President Development Economics
and Chief Economist

Mr. Richard Frank

BIS Conference

Richard, I'd be most grateful if you could give the
attached brief to Jim. A copy for you is also
enclosed. I hope it is helpful.

Many thanks

Michael

The World Bank
Washington, D.C. 20433
U.S.A.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

To James D. Wolfensohn

June 8, 1995

Dear Jim,

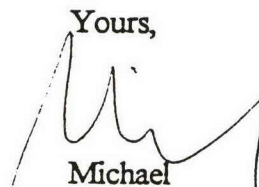
I am sorry I could not prepare the enclosed brief before you left. There was just too much to do and I had heard about the BIS conference and your trip only a few days ago.

I have enclosed a two-pager that reflects the talking points I used in recent seminars that I participated in - IDB in Jerusalem (with Cavallo, Summers and Frenkel) and a seminar that EDI in the Bank organized last week for some 30 high ranking Central Bankers from all over. Also enclosed are the relevant pages from our recent *Global Economic Prospects* (note in particular the interesting picture and Table on p. 17, contrasting Latin and East Asian economies); a photocopy of a February article on 'capital punishment' in the Economist, based on a paper of ours. Finally an update on private capital flows recently prepared by our International Economics Department.

Looking at the list of participants in the BIS seminar from emerging markets I know most of them in person (except for the gentlemen from Hong Kong, Malaysia, Riyadh and Venezuela). If you have the opportunity, I'd appreciate it if you could give them my regards, and also my regards to David Crocket, an old friend.

I hope you can now enjoy a quiet weekend in the Central Banking waters of Basle, having so dramatically (and, I believe, very constructively) stirred up the Bank during your first week in office.

Yours,



Michael

cc: Richard Frank, Jessica Einhorn, Masood Ahmed, Mark Baird

Living with Private Capital Flow volatility after Mexico: Talking Points
(used in recent seminars, April-May 1995)

1. One should differentiate between the main long-run driving force of private capital flows which is a stock adjustment phenomenon and between short-term flow volatility. The first is a portfolio diversification of savings of an aging population in the industrial countries looking for more profitable investment in emerging markets. This is very far from maturation. E.g., in 1913 the UK equity portfolio included 46% (!) in what were then emerging markets (20% were in Latin American markets). By contrast to-day only 1-2% of US pension funds are thus invested. This could easily rise to 5% over a decade implying a gross flow increase of 10-15% per annum (net flows may for a while increase by less, because of large current account deficits in LAC that will have to adjust). With time as the reform spreads the number and size of emerging markets will increase. Thus the process is bound to continue. Nonetheless in the short-run there is volatility of flows mainly driven by interest rate changes in the major industrial countries. This is a fact of life which is unlikely to change and has policy implications for the countries involved.
2. The composition of capital flows has changed with FDI now reaching 2/5 of the flows. Even in 1994 these increased by 19%, induced by continued trade liberalization, technical change, deeper reforms in host countries and globalisation of corporate production and distribution.
3. Regions differ and within regions countries differ widely in fundamentals, which are the main determinants of the response to capital flow volatility. Note the contrast in the recent *Global Economic Prospects* (Box 1-2, pp.16-17) between East Asia (excluding Philippines which is more 'Latin American') and between most of Latin America (with Chile more like an 'East Asian') in terms of the source of the current account deficit (whether originating from investment or consumption increase). The countries differ likewise in the share of FDI. It is important to point out that in 1994, despite rising interest rates and tough equity markets, equity and bond issues went up \$13 billion in East Asia while they went down by the same amount in Latin America. In 1995 FDI in total may not be very different from 1994. (For recent update on private capital flows see enclosed note from IEC.)
4. At this point in time one can say that our assessment in January that we were not in for a systemic crisis was correct. The contagion effect looked serious but the Mexican package helped. The crisis is now almost only confined to Mexico, in which a recovery is taking place, though the financial sector is still in deep trouble. The crisis may elsewhere have had a longer run sobering effect. In fact there were even some positive contagion effects - E.g., Cavallo used the Mexican crisis to pass reforms in parliament one month before the elections that he would never otherwise have brought about. Even the more drastic steps taken in Hungary recently can be attributed to the fear of a Mexico syndrome. There is hope that the investment funds and their clients have also learnt a lesson. In the future there are bound to be more single country crises, hopefully not of the same magnitude.

Major policy lessons

- a. Bad macro policy gets punished more quickly in the new global setting. The importance of macro fundamentals goes beyond fiscal discipline and highlights the need to watch the current account deficit (counter to the Nigel Lawson doctrine) and especially its roots (whether from investment or consumption increase).
- b. There is a high premium on private savings promotion, for example through introduction of mandatory savings schemes such as pensions (vide Chile).
- c. There is need to distinguish between keeping a fixed exchange rate as a nominal anchor during stabilization from high inflation (Mexico in 1988, Israel in 1985) and the need for greater exchange rate flexibility in face of capital mobility in more normal periods (a horizontal or diagonal exchange rate band provides an intermediate regime).
- d. The episode highlights yet again the importance of financial depth and healthy financial and capital markets with efficient regulatory and supervisory functions.
- e. As to Capital Controls - distinguish between countries that are opening up for which gradualism is advisable (especially if domestic financial markets are only gradually being liberalized) and between imposition of controls where they do not exist. These are in general distortive and may be effective only in the short-run. Our assessment is that Chile avoided trouble mainly because of its fundamentals and not so much due to its controls. (For more discussion see enclosed Economist summary of a DEC paper by Corbo and Hernandez, February 1995.)

Lessons for the IMF: mainly better surveillance and early warning system; less excitement about a new large lender of last resort facility.

Lessons for the World Bank: Greater emphasis on financial sector reforms so as to minimize pain once a crisis emerges. For countries that do not yet enjoy access to capital flows the reform process must be geared towards integration into the global economy. However there is a sequencing issue - the current account has to be opened up first (trade liberalization), fiscal conservatism is crucial and reasonably developed domestic financial markets are a good forerunner of capital account liberalization which in itself had better be undertaken gradually.

Fiscal consolidation and firm monetary policies should allow real long rates to move to the 4 to 4.5 percent range (rather than the 5 percent G-7 average at the end of 1994), implying, together with higher short-term rates, a flattening of yield curves. Real rates at this level imply that capital markets will remain tight. Additional fiscal consolidation could achieve larger reductions in long-term rates in the medium term, with beneficial implications for developing countries. It is estimated that a 1 percentage point reduction in interest rates sustained for five years could add 0.3 percentage points to developing countries' annual growth over that period, with growth effects as high as 0.5 percentage points a year in more indebted areas, such as Latin America and parts of Sub-Saharan Africa (Petersen and Srinivasan 1994).

Private capital flows: growth moderates

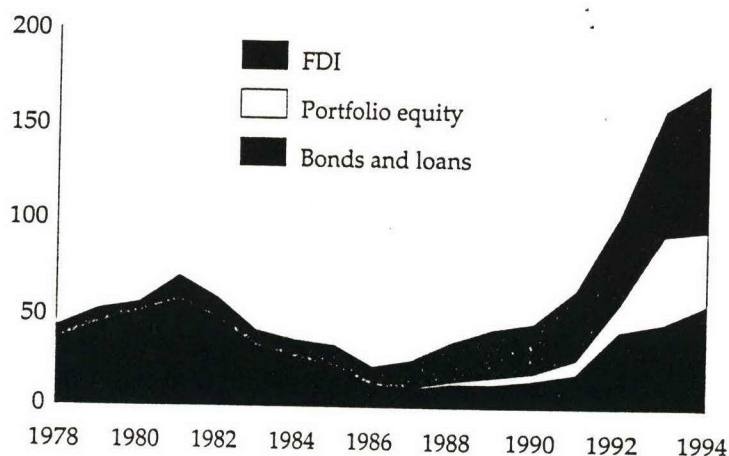
Growth in private capital flows to developing countries decelerated markedly in 1994, after having almost quadrupled in net terms in 1990–93 (figure 1-4). Flows to some countries in Latin America fell during the year. In Mexico the culmination was a balance of payments crisis that has, in turn, resulted in contagion effects on several Latin American stock markets and a correction in emerging markets in general. The Mexican crisis has renewed questions about the sustainability of capital flows to developing countries and the appropriateness of policies in dealing with them.

The crisis in Mexico is a result of problems that are largely specific to that country, as are recent balance of payments crises in Venezuela and Turkey. While in the latter two countries the underlying cause was serious fiscal imbalance, in the case of Mexico the main problem was the unsustainability of large and growing current account deficits. These resulted primarily from domestic rather than external factors. Significant domestic factors contributing to higher current account deficits included a fall in domestic saving rates and an appreciation of the real exchange rate (which was not sufficiently offset by higher productivity) in the wake of the surge in capital flows. In the past year concerns about political stability, loose monetary policy, an associated rise in off-budget spending through development bank lending, and the rise in U.S. interest rates helped trigger the crisis. Once confidence began to deteriorate, excessive reliance on short-term borrowing aggravated the looming liquidity problem.

While it is too early to draw general conclusions from the Mexican crisis, our analysis suggests that this is not 1982: a generalized reversal of private capital flows, as happened in 1982, is unlikely, the Mexican crisis notwithstanding. But major uncertainties continue to attach to the impact of the crisis on the state of financial market confidence and to the outlook for portfolio flows (on which Mexico was disproportionately dependent). In fact, Mexico alone accounted for about one-quarter of all portfolio flows to developing countries in 1993.

Private capital flows to developing countries slowed sharply in 1994, following rapid growth in 1991–93

Figure 1-4 Annual average net private capital flows to developing countries
(billions of dollars)



Flows	1977-82	1983-90	1991-3	1993	1994
FDI	8.5	16.0	50.2	66.6	77.9
Portfolio equity flows	0.0	1.3	22.9	46.9	39.5
Debt	42.9	17.7	35.2	45.7	55.5
Bonds	2.6	2.6	22.5	42.1	—
Loans	40.3	15.1	12.7	3.6	—
Total	51.4	34.9	108.3	159.1	172.9
<i>Memorandum items</i>					
Percent of GNP	2.4	1.0	2.4	3.5	3.6
Percent of exports	8.6	4.7	10.6	15.1	14.9

— Not available.

Source: World Bank data and staff estimates.

While the rise in flows in 1991-93 was supported in part by cyclical developments in industrial countries (low interest rates, weak economic activity), it was also underpinned by improved economic policies and prospects in most recipient countries. The importance of recipient country policies is reflected in the uneven distribution of private flows; in general, countries achieving greater progress in economic reforms have tended to attract more capital. The continuation and strengthening of reform policies in recipient countries should help sustain the flows. The higher returns on investment in developing countries, which attract foreign capital, are fundamentally supported by the stronger economic growth prospects of these countries. On the supply side, demographic shifts in industrial countries are likely to increase the pool of financial savings available for investment worldwide (see box 1-1).

The composition of private flows to developing countries has also become more diversified. Foreign direct investment (FDI), which is driven primarily by longer-term or structural factors, rose 17 percent in 1994, even as portfolio flows fell, and at more than two-fifths of private flows now accounts for the largest share. The increase in the share of non-debt-creating finance in total inflows provides a more favorable sharing of risk between recipients and investors than in the past. A further sharp rise in international interest rates on top of the 1994 increases would surely have a serious effect on private flows, but as noted in the preceding section, such an increase seems unlikely. Overall, private capital flows to developing countries are likely to continue to increase in the medium term, though at a much slower pace than in the early 1990s.

FDI flows should continue to rise with the further globalization of corporate production and distribution strategies induced by trade liberalization, technological change, and deeper reforms in an increasing number of host countries. In addition to finance, these flows bring important supplementary benefits in technology and export market development. Higher projected growth in developing regions such as Africa and Eastern Europe and the former Soviet Union should encourage more flows to countries there than in the past, reducing the current concentration of private flows in a few countries. A recent study (Bhasin, Jun, and Economu 1994) finds host country growth the single most important determinant of FDI inflows: a 1 percentage point increase in the average GDP growth rate of developing countries is found to raise FDI inflows, at current levels, by about \$10 billion. Gross FDI flows have risen as a share of developing-country exports and domestic investment by 4 to 5 percentage points since 1988. If these ratios rise by, say, 2.5 percentage points in the next decade as a result

of further international integration, FDI to developing countries would rise by 10 to 15 percent a year, or 7 to 12 percent in real terms, compared with average annual real increases of 39 percent in 1991-94 and 11 percent in 1981-90.

Portfolio flows will no doubt go through a period of stagnation after the Mexico crisis. However, once confidence is reestablished, growth in portfolio flows to developing countries is likely to be supported by growth in global financial assets, growth in developing countries' exports and capacity to service foreign liabilities, continued development of capital markets in developing countries, and increased diversification of investor portfolios. Global equity market capitalization increased fivefold between 1984 and 1994 to \$17.8 trillion, with the share of emerging markets rising from about 4 percent to 10 percent. A conservative projection would be for global equity market capitalization to at least double by 2004, with the share of emerging markets rising to more than 20 percent.⁷ At the same time, the share of developing countries in investor portfolios in industrial countries can be expected to increase from its still very low level (about 1 to 2 percent of U.S. pension fund financial assets are currently invested in emerging markets). Assuming an increase in this share, on average, to 5 percent (much less than the 20 percent or so typically suggested by optimal risk-return calculations), the stock of developing-country equity held by foreigners could increase fivefold over the next decade, with gross flows again rising on average by 10 to 15 percent annually in nominal terms.

Net private capital inflows are expected to grow less rapidly than gross flows, depending on the current account paths of different developing countries and regions. Many countries are at the limit of prudent borrowing, so at most their net liabilities can rise in line with exports. Current account deficits in Latin America, Sub-Saharan Africa, and the Middle East and North Africa, in particular, are expected to be reduced to more sustainable levels. Given projected trends for current account deficits, official financing, and reserve accumulation, net private capital flows are expected to grow on the order of 7 to 10 percent a year over the next decade. Within this overall trend Asia and several transition economies are likely to see the largest increases, while private capital flows to Latin America are likely to grow at a slower pace as a result of current account adjustments in the wake of the Mexican crisis.

Although a generalized reversal of the increased private capital flows to developing countries appears unlikely, individual countries may be vulnerable to volatility in flows, depending on their circumstances. The risk of volatility has been heightened by the Mexican crisis. Maintaining strong economic funda-

mentals is the key to ensuring stability and steady growth in private capital inflows. When a reversal of inflows occurs, as recently in Mexico, it may appear to be sudden, but its causes can be traced to slippages in economic policy and performance. Despite the extreme reaction of financial markets to the devaluation of the Mexican peso, the unsustainability of Mexico's current account deficit and the need for adjustment had been widely recognized.⁸ A number of early warning signs had signaled impending trouble. A lesson from the Mexican crisis is for policymakers to pay particular attention to such advance warnings of looming problems.

One important indicator of an emerging crisis in capital flows is a large appreciation of the real exchange rate. The appreciation often arises from persisting too long with a fixed nominal exchange rate introduced as part of a stabilization program and is aggravated by large capital inflows attracted by the high interest rates needed to support the exchange rate. Other signals to watch for, and often associated with a substantial real exchange rate appreciation in the capital-recipient country, include a declining domestic saving rate (indicating that the inflows are going into consumption rather than investment), inadequate investment in the tradables sector, weak export growth, and a rise in current account deficits to levels that are inconsistent with prudent targets for foreign liabilities (given such factors as initial debt levels, expected interest rates, and the size, growth rate, and volatility of exports). Another warning indicator is a growing reliance on short-term capital inflows. Though country cases differ and no one indicator is infallible, monitoring a combination of these indicators can help in detecting an emerging balance of payments crisis and in initiating timely adjustments. Given the speed at which capital can move in and out of countries today, there is an increased premium on sounder, more agile economic management.

The current international economic environment provides a favorable setting for capital-recipient countries to reduce their vulnerability to volatility in private flows by strengthening their economic fundamentals. Adjustment is necessary in countries where the rise in inflows has been associated with unsustainable increases in current account deficits. Boosting export growth is central to achieving a soft landing for external deficits. Failure to adjust carries the risk of undermining market confidence and triggering an abrupt reversal of inflows that would force a hard landing. In assessing capacity to service rising external liabilities, countries need to allow for both debt and nondebt external obligations: FDI and other equity inflows bring important benefits but also tend to require higher returns. Among major recipients the need to adjust to a slower growth in external liabilities is in general great-

est in Latin America (box 1-2). This need has been underscored by the Mexican crisis.

The mix of policies appropriate for fostering sustained private capital inflows depends on a country's circumstances. The intensity of the undesirable macroeconomic side effects of inflows, such as overheating and real exchange rate appreciation, varies with the behavior of private savings, growth in productivity, and other factors. But cross-country experience offers some general policy lessons. These point to the importance of fiscal restraint, structural reforms that guide resources toward investment and exports rather than consumption, and a sound institutional and regulatory framework for the banking system and capital markets.

World trade: developing countries lead a marked acceleration

World merchandise trade (exports plus imports) surged by an estimated 8 to 9 percent in 1994, up from about 4 percent in the 1991-93 recession. Trade growth is expected to continue at a brisk pace through 1996. Trade in services should grow even faster, partly because of higher flows of foreign direct investment, increasingly directed at the services sector, and growth of long-distance services (see chapter 3). In the longer run (1997-2004) merchandise trade growth is projected at about 6 percent, roughly the same as in 1986-90. Supported by a shift toward outward-oriented policies that are increasing their integration in the world economy, trade growth in developing countries is expected to exceed that of industrial countries by 1 to 1.5 percentage points.

This forecast represents a continued trend toward more rapid global trade integration that took hold in the mid-1980s (table 1-4).⁹ This, in turn, may represent a resumption of the trend of the 1950s and 1960s before the macroeconomic instabilities of the 1970s and early 1980s—the twin oil shocks and the debt crisis. Six factors underpin the expected strength of world trade growth: in the nearer term (1995-96) the cyclical recovery in industrial countries, yen appreciation and market opening in Japan, and the increased purchasing power of primary exporters from higher commodity prices; in the longer term faster growth in developing countries, integration of world capital markets (reflected in the rise of private capital flows to developing countries), and accelerated trade liberalization, including the extension of regional trading arrangements to encompass some developing countries.

In a remarkable departure from historical relationships, world trade continued to grow by about 4 percent in 1991-93, despite the recession in industrial countries. This contrasts with previous recessions in

Box 1-2 Contrasts in managing capital inflows: a tale of two regions

The recent surge in private capital flows has been concentrated in East Asia and Latin America, but there are several differences between the two regions in the composition and management of the flows. These differences, brought into sharper relief by recent developments in Mexico, have important implications for future flows to these regions and for policies for managing the flows.

While regionwide macroeconomic indicators mask appreciable variations among countries (with Chile's performance, for example, resembling that of successful East Asian countries), they nevertheless reveal some important differences between the two regions (inset table). East Asia has underpinned larger inflows with a more stable macroeconomic environment that is more favorable to sustained high growth. East Asia has maintained high national saving and investment rates, exceeding those in Latin America on average by as much as 13 percent of GDP. Higher investment and GDP growth in East Asia (where growth averaged 7 percent in 1990-93, compared with 2.4 percent in Latin America) has been primarily domestically financed. Complementing domestic savings, inflows into East Asia have tended to increase investment rather than consumption, while in some countries in Latin America the inflows have fed a consumption boom (inset figure). The average national saving rate in Latin America fell in the 1990s, the period of high capital inflows, but rose in East Asia.

East Asian export growth has been stronger, and exports represent a much larger share of GDP, signaling a better future capacity to service foreign liabilities. Foreign liability to export ratios in Latin America substantially exceed those in East Asia and have risen as the increase in inflows outstripped the growth in exports. East Asia has continued to provide investors and exporters with a more stable financial environment, reflected in both lower inflation and a lower variability of inflation and real exchange rates than in Latin America. East Asian countries (except the Philippines and Thailand) have also avoided significant appreciation of real exchange rates, thereby protecting external competitiveness, despite larger capital inflows. Real exchange rates appreciated significantly in several Latin American countries, despite efforts to mitigate the impact of capital inflows through sterilization or, in some cases, capital controls. The erosion of competitiveness was in turn associated with rapidly widening current account deficits. In East Asia's comparative success in avoiding real currency appreciation, the higher proportion of FDI in total inflows and the channeling of more inflows to investment have been contributory factors. In general, East Asian countries have also made greater use of fiscal restraint in coping with inflows (Corbo and Hernandez 1994).

East Asia has also attracted a more favorable mix of flows. In 1990-93 FDI constituted about 55 percent of net private flows to East Asia, compared with about 40 percent for Latin America. Within portfolio investment, equity flows accounted for about 55 percent of the total in

East Asia and 45 percent in Latin America. Most FDI in East Asia has been in new investments—greenfield operations and joint ventures. In Latin America FDI has been associated largely with privatization of enterprises, which raised almost \$17 billion in foreign exchange between 1988 to 1993 (only \$5 billion in East Asia), and debt-equity swaps. The higher inflow of FDI into East Asia has been supported by higher returns. Estimated average returns on U.S. FDI in East Asia in 1990-93 were more than twice the average worldwide return on U.S. FDI, while returns in Latin America were only slightly higher.

Given East Asia's stronger economic fundamentals and sounder macroeconomic responses to large capital inflows, the likelihood of capital flows being sustained is higher for countries in this region than in Latin America. Latin American countries, such as Mexico, experiencing large increases in current account deficits need to adjust to lower capital inflows. East Asia's greater success in attracting non-debt-creating and longer-term flows also makes it less vulnerable to volatility in flows. Evidence of the greater resilience of East Asian inflows to external shocks is provided by the behavior of portfolio flows in 1994. Despite rising international interest rates and difficult bond and equity market conditions, East Asian countries were able to increase their international equity and bond and debt issues by more than \$13 billion, compared with a drop of \$8 billion for Latin American countries.

East Asia has underpinned larger capital inflows . . .

Total private capital inflows (annual average post-cutoff date)

Region/ country	Cutoff date	Amount (\$ billions)	Percent of 1992 GNP
<i>Latin America</i>			
Brazil	1991	5.8	1.5
Argentina	1991	5.4	2.4
Colombia	1993	1.3	2.7
Venezuela	1991	1.8	3.0
Costa Rica	1991	0.2	3.1
Mexico	1990	11.8	3.7
Chile	1990	1.6	4.2
Average		4.0	2.9
<i>East Asia</i>			
Korea, Rep. of	1991	6.6	2.2
Philippines	1992	1.4	2.6
Indonesia	1990	3.7	3.0
Thailand	1988	4.5	4.2
China	1992	27.6	6.4
Malaysia	1989	4.1	7.5
Average		8.0	4.3

Source: World Bank and IMF data.

... with stronger economic fundamentals

Macroeconomic indicators: Latin American and East Asian countries

(annual means for individual countries)

Region/ country	GDP growth (%)	Gross national savings (% GNP)	Gross domestic invest- ment (% GNP)	Govern- ment con- sumption (% GNP)	Total exports (% GNP)	Annual export growth (%)	External debt/ exports (%)	Monthly inflation variance (%)	Monthly REER ^a variance (%)	Monthly inflation (%)	REER ^a appre- ciation (%)
<i>Latin America</i>											
Brazil	0.7	21.7	21.5	14.1	11.8	4.3	303.7	—	—	26.0	-5.9
Argentina	3.5	17.3	19.3	8.4	10.9	4.1	478.3	—	—	16.4	151.8
Colombia	3.6	22.5	19.6	12.1	19.3	6.6	167.2	0.7	3.1	1.9	14.6
Venezuela	2.7	20.0	16.5	9.2	25.4	6.0	181.8	7.7	19.4	3.1	3.8
Costa Rica	5.1	20.1	29.2	17.6	40.2	10.7	208.8	0.5	1.4	1.4	-10.2
Mexico	2.6	17.6	22.8	9.3	20.3	3.1	223.9	3.5	8.0	1.7	40.7
Chile	7.1	25.2	28.1	10.4	35.4	11.1	207.4	0.7	2.4	1.3	9.5
Average	3.6	20.6	22.4	11.6	23.3	6.6	253.0	2.6	6.9	7.4	8.7 ^b
<i>East Asia</i>											
Korea, Rep. of	7.1	36.4	37.6	7.1	31.1	9.5	44.8	0.2	6.0	0.5	-10.0
Philippines	1.0	20.6	22.6	9.5	32.0	6.2	226.0	0.4	15.8	0.9	6.9
Indonesia	6.6	33.3	35.6	6.6	24.1	6.1	221.7	0.7	1.4	0.7	-4.1
Thailand	9.5	32.1	37.6	9.5	34.3	17.3	140.7	0.4	1.6	0.3	7.1
China	8.9	46.5	44.9	9.7	19.4	14.6	86.2	0.1	2.3	0.8	-12.6
Malaysia	8.8	31.8	32.2	14.3	73.7	13.1	66.2	0.1	3.4	0.3	-12.5
Average	7.0	33.5	35.1	9.4	35.8	11.1	130.9	0.3	5.1	0.6	-6.6

— Not available.

Note: Estimated over a period starting two years before significant inflows began (the cutoff date) and ending in 1993.

a. Real effective exchange rate.

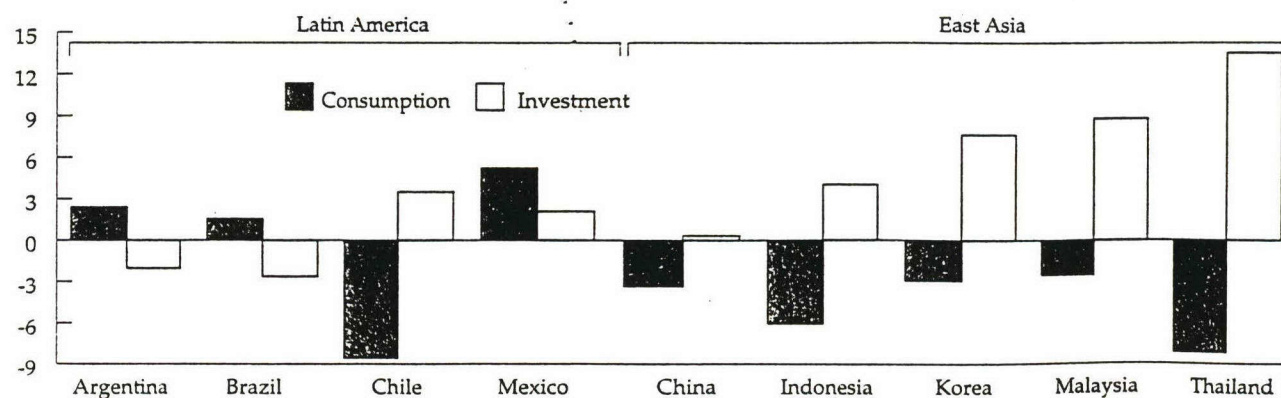
b. Excludes Argentina.

Source: World Bank and IMF data.

Inflows into East Asia have tended to increase investment rather than consumption

Change in consumption and investment between 1985-87 and 1991-93

(percent of GNP)



Note: The years 1985-87 represent the period before the inflow and 1991-93 the period after the inflow began. For Korea, the average for the second period includes only 1991-92.

Source: World Bank staff estimates.

Capital punishment

Should developing countries try to control short-term capital inflows?

WHILE the world digests the implications of this week's rescue of Mexico, the issue of controlling capital inflows may seem oddly arcane. It is not. Although foreign capital is unlikely to be surging into emerging economies this year, the long-term consequences of the Mexican crisis will depend, in part, on how developing countries treat inflows of foreign capital, and particularly portfolio capital (stocks, bonds, etc), in future.

Look at the emerging economies that have been least affected by the recent investor panic and you see the dilemma. A country such as Chile, which has some controls on short-term capital inflows, has been less affected by market jitters than one such as Argentina, where foreign investors hold significant amounts of shares and bonds. Does this mean that developing countries should rethink their enthusiasm for foreign capital?

Most economists agree that removing capital controls can be dangerous if an emerging economy has not yet liberalised prices and trade. In that case, large inflows of foreign money serve only to promote the wrong sorts of investment and output. Many argue that the removal of capital controls should therefore come towards the end of the process of economic reform. It may make sense, for instance, for the former communist countries of Europe to retain some of their capital controls for a time. But why does a country such as Chile, which is widely regarded as the most advanced of the Latin American reformers, need to employ such controls, albeit of a limited sort?

It is worried that short-term capital inflows might undermine the competitiveness of its economy. The main goal of

ECONOMICS FOCUS

Chile's macroeconomic policy is to maintain a competitive real exchange rate. A key pillar of its economic success over the past decade or so has been the liberalisation of the economy and an increase in exports. The competitiveness of Chilean exports was strongly supported by a depreciating real exchange rate: between 1982 and 1988 it fell by 53%.

Large inflows of foreign capital make it more difficult for the government to control the real exchange rate. When the Chilean economy was showing signs of overheating at the beginning of the 1990s, for instance, the central bank raised real interest rates. The effect of such a rise, however, was to attract large amounts of foreign capital: Chile's foreign-exchange reserves rose by almost 70% in 1990 alone. This enormous capital inflow pushed up the real exchange rate.

Worried by the prospect of a further real exchange-rate appreciation caused by short-term capital inflows, Chile at first tried to neutralise their effect by selling domestic bonds, but without much success. Since 1991 the Chilean approach has been to allow some real appreciation, by revaluing the exchange rate (see chart). But Chile has also tried to limit the inflow of capital.

Among other things, it has tried to increase the exchange-rate risks facing foreign investors by widening the band within which the currency can fluctuate; it has swept away restrictions on capital outflows; and it has also introduced specific measures to discourage capital inflows, including a special stamp tax and high

minimum reserve requirements on foreign credits.

Although its reputation as a model reformer makes the Chilean case particularly striking, it is not the only emerging economy to impose such restrictions on capital inflows. Throughout Asia, restrictions on foreign borrowing by domestic companies and higher reserve requirements on foreign inflows are common. In the short run, these controls do make it easier to maintain a stable real exchange rate, as a recent World Bank study* has strikingly confirmed.

However, a competitive real exchange rate, as opposed to a stable one, is better achieved by keeping fiscal policy tight and interest rates low. And an exchange rate that is both stable and competitive is not the only goal of economic policy. Capital controls can make it harder to achieve other goals, and the tighter the controls the greater the cost.

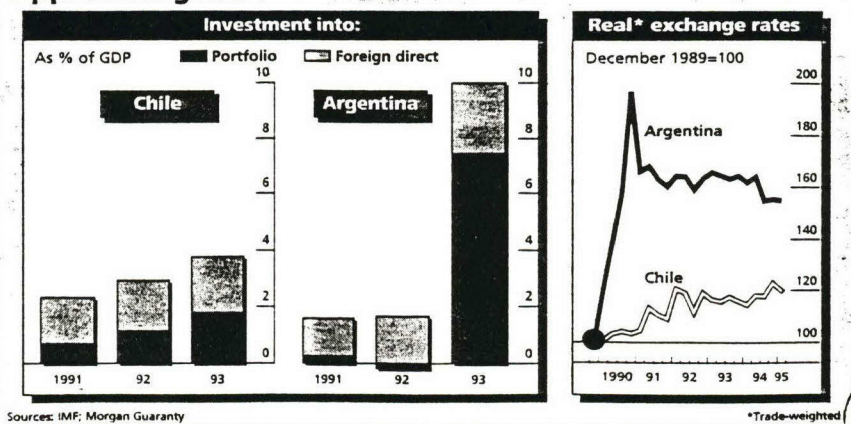
Mobile money

Capital mobility, like free trade, results in the most efficient allocation of global resources. By allowing investors to put their money where it will earn the highest rates of return, the world as a whole makes the best use of its savings. Capital controls prevent this from happening. As well as denying a country access to the cheapest possible sources of finance, capital controls also have other nasty side-effects, such as preventing a country's domestic financial system from becoming more efficient. Worse, as investors find ways around them, the scope of controls may have to be increased, causing further distortions.

For all of these reasons, it would be wrong to conclude that capital controls are a sensible long-term policy, although some restrictions may be appropriate for countries in the early stages of economic reform, or as a temporary measure when large amounts of foreign capital flood in unexpectedly. Many developing countries would indeed do well to copy the Chilean model. But Chile's restrictions on short-term capital inflows are hardly the key to its success. Its commitment to liberalisation and deregulation, not its penchant for capital controls, has made it Latin America's most successful reformer. And in Chile at least, notwithstanding recent events, such controls may have outlived their usefulness.

* "Macroeconomic Adjustment to Capital Inflows", by Vittorio Corbo and Leonardo Hernandez. World Bank Policy Research Working Paper No 1377

Appreciating Chile



Update on Private Capital Flows Post-Mexico

1. Private capital flows to developing countries over the past year have been affected by two main factors: the turning point in US interest rates in February 1994 and subsequent increases through the year, and the Mexico crisis. The deceleration of flows to developing countries has been on account of portfolio flows alone. FDI flows continued to increase in 1994, as did commercial borrowing.

- Portfolio flows--both equity and bonds (based on data of international issues) which decelerated during 1994 primarily because of the interest rate increases, declined sharply after Mexico. In the first quarter of 1995, international equity flows were only US\$ 0.5 billion, compared to an average of US\$ 4.9 billion during 1994, and bond issues were only US\$ 5.5 billion compared to an average of US\$ 12.5 billion in 1994. (Note that these data do not include direct participation in equity markets).

- Although no data are available, our best assessment is that FDI flows to developing countries in aggregate over the first few months have not been affected.
- Commercial loans also appear to have been affected only minimally.

2. Underlying these trends in capital flows has been considerable differentiation between countries and regions. From the stock market index, it would appear that while portfolio flows have been negative in the first quarter in all regions, the declines have been much more pronounced in Latin America than in Asia (see graphs). Moreover, since portfolio flows have accounted for a larger part of total private flows to Latin America, the impact on aggregate private flows to Latin America has been sharper than on East Asia. The differentiation of borrowers on the part of creditors is also evident in the risk spreads on international bond issues. All developing countries saw a rise in spreads over US dollar denominated fixed rate issues, as rising interest rates have made investors particularly sensitive to credit risks—but Latin America saw a 100 bp widening of spreads in 1994, whereas Asia saw a widening of about 48 bp.

3. Most recent trends indicate an upturn in stockmarkets in developing countries, reflecting greater confidence on interest rate outlook and a gradual recovery of confidence post-Mexico (see graphs). April-mid May data on international issues of equity and bonds also show a sizable pickup in activity. (International bond issues over April-mid May have risen by 11% compared to the average of the first quarter, while equity issues during the past one and a half months—at US\$ 652 million—have been higher than over the entire first quarter—at US\$ 488 million).

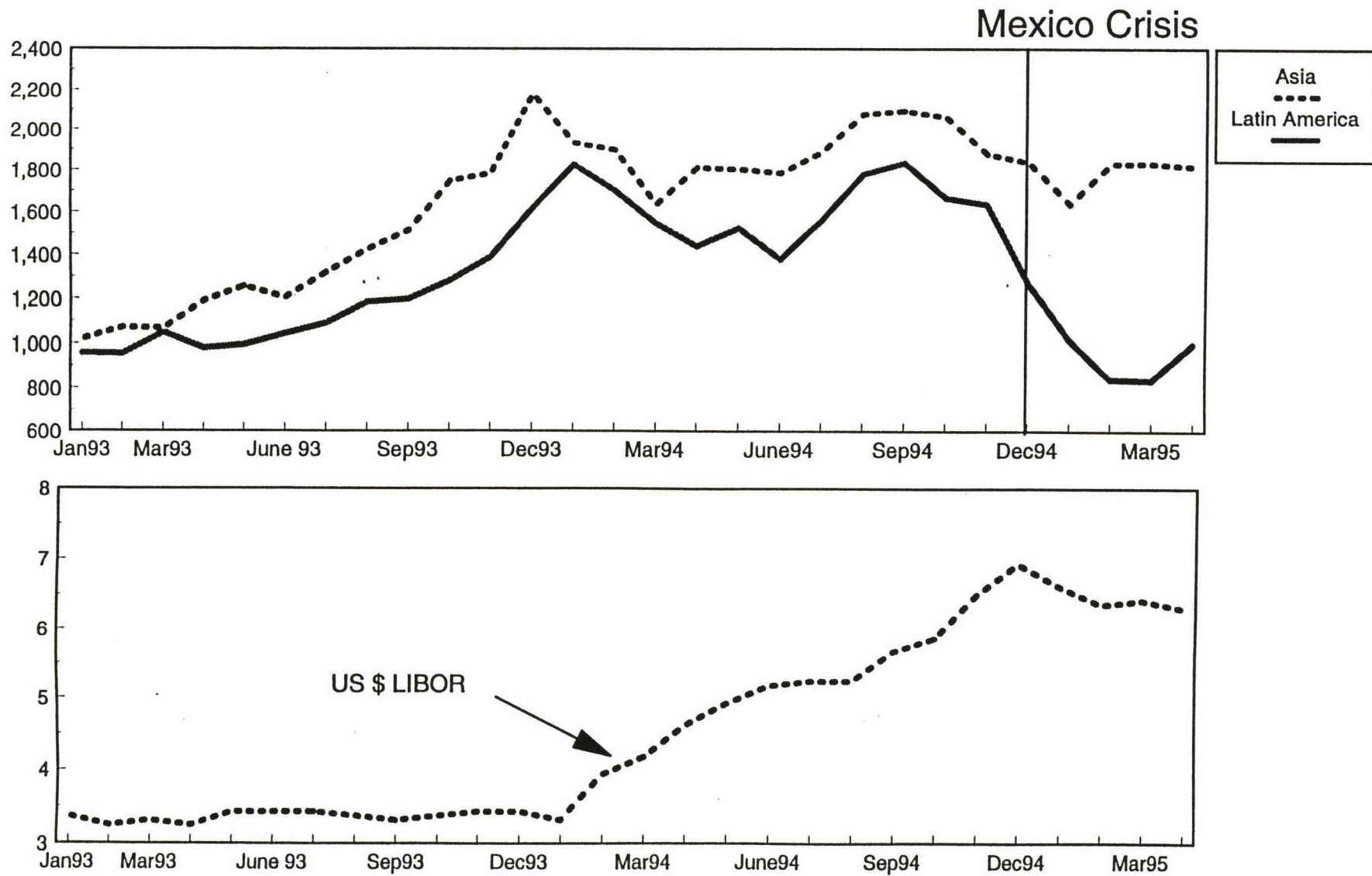
4. At this juncture there is, of course, still considerable uncertainty as to what the outcome will be for 1995. If we extrapolate from first quarter trends, and assume that FDI¹ and loans flows will stabilise at their 1994 levels, then private capital flows could decline by about ~~26-30%~~ from their 1994 levels.

around a third !

swati\ d:\wrd6\doc\postmex.doc

¹ FDI flows to developing countries in 1995 could in fact be somewhat lower than 1994, in light of a deceleration in flows Mexico (which saw a surge in 1994 following the NAFTA agreement) and China (which received as much as 30 billion in 1994, and may be reaching absorption constraints). On the other hand, first quarter data on US FDI to Latin America shows a 46% increase relative to the first quarter of 1994.

IFC Price Index



The World Bank

1818 H Street, N.W.
Washington, D.C. 20433, U.S.A.



June 8 1995

With the compliments of

Michael Bruno

Vice President Development Economics
and Chief Economist

Mr. James Wolfensohn

Jim,

As promised, here is Larry Summers' paper on
educating girls.

Best,

Michael

Policy Research

WORKING PAPERS

Development Economics

Office of the Vice President

The World Bank

May 1992

WPS 905

Investing in *All* the People

Lawrence H. Summers

Money spent increasing the education of girls is not only more socially productive than military outlays. It is also far more productive than other social sector outlays — and than the vastly larger physical capital outlays projected for the next decade.

The World Bank
Washington, D.C. 20433
U.S.A.

Chen J.W

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

June 5, 1995

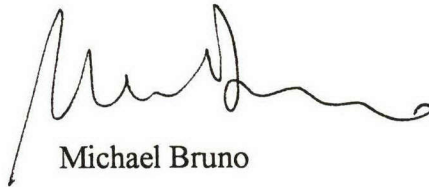
Mr. James D. Wolfensohn

Update on Bank-Fund-WTO Collaboration

Jim,

As promised, attached is an update on issues of Bank-Fund-WTO Collaboration. This may be relevant to your lunch with Mr. Camdessus on June 6.

I suggest that we spend 15 minutes between now and lunch tomorrow for a quick briefing on more likely issues that may come up at the lunch.



Michael Bruno

Attachment

cc: Managing Directors
Ms. Horiguchi

Bank-Fund-WTO Collaboration: An Update

Although we have had no communication from the WTO Secretariat about your meeting with Mr. Ruggiero on June 13, we understand that the Fund have received an indication of the issues Mr. Ruggiero wishes to raise at the corresponding meeting with Mr. Camdessus. We understand that Mr. Camdessus hopes that the Bank and the Fund will be able to maintain largely common positions in their dealings with WTO, and that as a result he may raise some of these issues when you meet him on June 6. There should be no difficulty in reaching a common understanding with Mr. Camdessus.

The WTO Secretariat has suggested that the following four issues may arise:

- (a) Mr. Ruggiero is likely to suggest that the WTO play an active role in the Development Committee and that the latter become the principal locus for dealing with coherence in global economic policy making.

We would counsel against this. As you know, there is a growing consensus that the role of the Development Committee needs to be

rethought. However, it is not obvious that broadening it further is the right way to go. Moreover, it seems sensible to define coherence before locating it. Effective, as opposed to ceremonial, treatment of coherence seems far likelier to be achieved through staff and management interaction than in a political body such as the Development Committee.

- (b) Mr. Ruggiero will suggest that a joint Bank-Fund-WTO communiqué be issued prior to the Halifax meeting.

Mr. Camdessus is expected to reply that this is neither a traditional nor an effective way of communicating with the G-7. We agree.

- (c) Mr. Ruggiero wishes to discuss the reform of the G-7, possibly arguing that it should be made more broadly representative and that the Bank, Fund and WTO should have greater direct input.

Mr. Camdessus is unsympathetic to this proposal, favoring, in particular, a more prominent role for the Fund and its Interim Committee. It is not clear that the Bank has a direct interest in either of these proposals, and we suggest that you should be noncommittal

about both. Since Mr. Ruggiero's (predicted) views are unlikely to prevail, and since, if they did, they would doubtless entail the promotion of WTO interests above those of the Bank, it seems particularly desirable not to become associated with that.

- (d) Consideration will also be given to the state of discussions about cooperation between the Fund and WTO. These are formally somewhat more advanced than discussions between the Bank and WTO, but are still held up by significant differences both between the Fund and the Secretariat and between the Secretariat and the member governments of WTO. Fund staff keep us informed of the progress of their discussions, which we appreciate, and they are also sympathetic to our view that Fund-WTO and Bank-WTO discussions on cooperation should proceed broadly in parallel. It may be useful to reaffirm this with Mr. Camdessus.

Mr. Camdessus may suggest that he and Mr. Ruggiero issue a press statement to the effect that discussions on collaboration between the staffs and managements of the two institutions are progressing well and that they will shortly present to their Board and General Council a draft agreement. It would unfortunate if such a statement were made and we were unable to match it. It

would be desirable if Mr. Camdessus expressed the wish that the Bank also be party to such a statement and would lend his weight to persuading Mr. Ruggiero that the Secretariat should be forthcoming enough in its discussions with us to allow us honestly to subscribe to such a statement.

[IECIT\k:\jwb\brief3.doc(2-Jun-95)]

OFFICE MEMORANDUM

DATE: June 2, 1995

TO: Mr. James D. Wolfensohn

FROM: Michael Bruno *MB*

EXTENSION: 33774

SUBJECT: **Bank-Fund Collaboration on Public Expenditure Work**

1. The overall level and distribution of public expenditure is one of the key instruments available to government policymakers. Government's handling of public finances is a key determinant not only of financial viability but also of the efficiency and equity with which scarce resources are allocated within an economy. In particular, analysis of public expenditure priorities, and the government's capacity to deliver quality services, is a critical element in shaping the country's overall development effort. For the Bank's work with its clients, public expenditure analysis serves many purposes: supporting the policy dialogue, identifying areas for capacity building, helping shape social policy and providing a framework for the Bank's lending and aid coordination efforts. The Fund also relies heavily on the Bank's public expenditure work for the design of its own policy advice. Collaboration in this area has generally been good but much depends on staff personalities on both sides. Fund staff have expressed some concerns about the timeliness of the Bank's public expenditure work and its consistency with the Fund's macroeconomic framework. Bank staff, in turn, have been concerned that they do not always have adequate access to and involvement in the Fund's macro and fiscal work.

2. Over the past year the Bank has been reviewing its public expenditure work. This was partly motivated by a general concern to assess Bank efforts in this area and see where improvements could be made. Fund staff had also produced a Task Force Report so there was an opportunity to review Bank and Fund staff involvement and collaboration in these issues. At a lunch meeting between Mr. Preston and Mr. Camdessus in October 1994, both staffs were asked to examine the issues raised in these reviews. It was also agreed that a draft note would be prepared for the two managements' signatures to provide staff with a clearer indication of expectations in this area.

3. Since then, Bank staff has completed its internal report on public expenditure work and established its own task force on these issues. The institutions have shared their reports, and pilot cases have been identified to discuss priorities for and issues in public expenditure work. The first regional meetings (AFR and ECA) have taken place, and the country pilot cases (Cote d'Ivoire, Lithuania, and Zambia) are underway.

4. Based on the Bank and the Fund reports and the subsequent discussions, we suggest that a joint guidance note be sent from the two managements to the staffs of the two institutions, which we attach for your approval. It has been reviewed by the two institutions' interdepartmental task forces on public expenditures. It suggests:

- annual meetings between the regional and area department senior staffs of the Bank and the Fund, to review experience with previous efforts and to identify priorities for future work on public expenditure (including related fiscal and institutional development issues);
- country-by-country collaboration, to assess ongoing efforts and to define immediate priorities;
- possibilities of requests by Fund staff on short notes on specific public expenditure issues from Bank staff, and of requests by Bank staff on recent fiscal analysis and macroeconomic projections prepared by Fund staff; and
- joint analytical work on selected public expenditure issues.

5. A similar note has been sent by Fund staff to their Management. You might want to discuss this issue with Mr. Camdessus during your lunch on June 6. After this, and with your agreement, we propose to distribute the attached joint guidance note to Bank staff.

cc: Mr. Kaji

EXTERNAL MAIL
JDW

EXTERNAL

A

P. LIVINGSTONE ARMSTRONG

1173 FECHY
SWITZERLAND

1357A
TELEPHONE (021) 808 5535

FAX (021) 808 6441

PLA/SF/6092

COPY

95 JUN 28 PM 3:45

RECEIVED
DEVELOPMENT ECONOMICS
VP & CHIEF ECONOMIST

cc. Mr. Lyn Square

The President,
Oxford University Press Inc.
200, Madison Avenue,
New York, NY 10016, USA.

14th June, 1995

Dear Sir,

Report IBRD - "Adjustment in Africa, 1994"

In preparing a proposal for discussion with the World Bank, it is observed that your prior permission to use data in quoting from the above must be requested.

As such use, and permission, is urgently needed, your earliest attention will be greatly appreciated.

Sincerely,



P. Livingstone Armstrong.

Copy to The President, World Bank,
1818 H Street, NW,
Washington, DC 20433, USA.

COPY

P. LIVINGSTONE ARMSTRONG

1173 FECHY
SWITZERLAND

TELEPHONE (021) 808 5535

FAX (021) 808 6441

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95 JUN 27 PM 4:00
RECEIVED
DEVELOPMENT ECONOMICS
VP & SENIOR ECONOMIST

The President,
Oxford University Press, Inc.,
200, Madison Avenue,
New York, NY 10016, USA.

14th June, 1995

cc. *Vicente Sogui*

Dear Sir,

Report IBRD - "World Development Report, 1994".

In preparing a proposal for discussion with the IBRD (World Bank) it has been observed that your prior permission to use data in quoting from the above must be requested.

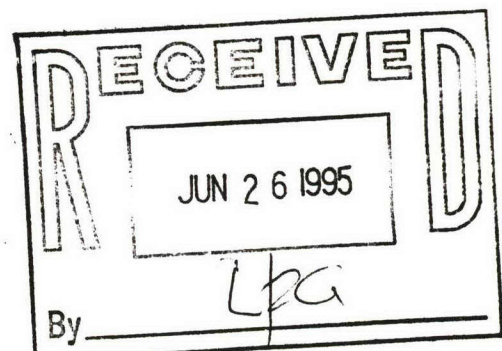
As such use, and permission, is urgently needed, your earliest attention will be greatly appreciated.

Sincerely,



P. Livingstone Armstrong.

Copy to The President, World Bank,
1818 H Street, NW,
Washington, DC 20433, USA.



COPY

B

C

J. W. Chiron

MASOOD AHMED
Director
International Economics Department

May 31, 1995

Ms. Pinky Chaudhuri
2480 16th Street, NW # 512
Washington, DC 20009

Dear Ms. Chaudhuri:

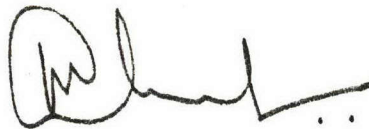
Mr. Wolfensohn's office has passed on to me your letter of May 15 expressing an interest in joining the World Bank to work on international trade issues.

I agree with you that international trade is indeed a major issue of international economic development and I also share your view that the World Bank should continue to play an important role in this area.

You may not be aware, however, that we have already set up an International Trade Division which has as its principal objective, the carrying out of research, policy advice, and operational support on trade issues. This division also supports the Bank's Senior Management in ensuring that trade issues are adequately reflected in our country strategy work and in providing coordination of trade related issues with other multilateral agencies. Given these circumstances, we do not see the need to create a new position for an International Trade Coordinator at this time; nor do we have any other current vacancies in the international trade area which would appear to fit your training and background. If you are interested in contributing to the Bank's work in other area, please let me know and I will be happy to pass on your resume to the appropriate people.

In the meantime, I would like to thank you for your interest in the work of the Bank.

Sincerely,



Masood Ahmed

bcc: Mr./Mmes. M. Aniba, J. Bassinette, C. Oram, A. Winters

THE WORLD BANK GROUP

ROUTING SLIP		DATE: May 26, 1995	
NAME			ROOM. NO.
Mr. Masood Ahmed			S9-035
☐	URGENT	☐	PER YOUR REQUEST
☐	FOR COMMENT	☐	PER OUR CONVERSATION
☐	FOR ACTION	☐	NOTE AND FILE
☐	FOR APPROVAL/CLEARANCE	☐	FOR INFORMATION
☐	FOR SIGNATURE	☐	PREPARE REPLY
☐	NOTE AND CIRCULATE	☐	NOTE AND RETURN
☐		☐	
RE: Attached			
REMARKS: Masood, I am sending this to you both in your acting capacity and as Director IEC. Could IEC prepare an appropriate response? I leave it to you to decide whether it should go under Michael Bruno's name or yours. As Ms. Chaudhuri has called this office 3 times asking if EXC had passed her correspondence to us (it just arrived now) and also I believe called EXC a couple of times, we should try and get a reply to her as soon as possible--say by Friday, 6/2. (Please see EXC note re copies.). Many thanks. Kate (Ms. Chaudhuri said she would call me again next Wed. May I transfer the call to you or Alan? She may be sensitive as to level.)			
FROM Kate Oram		ROOM NO. S9-035	EXTENSION 31107

THE WORLD BANK GROUP
Headquarters: Washington, D.C. 20433 U.S.A.
Tel. No. (202) 477-1234 • Fax (202) 477-6391 • Telex No. RCA 248423

FACSIMILE COVER SHEET AND MESSAGE

DATE: May 26, 1995

NO. OF PAGES: 4
(including cover sheet)

MESSAGE NO.: {#}

TO: Kate Oram

Mr. Ahmed

DESTINATION FAX NO.: 70549

FROM: Marce T. Aniba, EXC

Room No.: E1227

Telephone: 84138

SUBJECT: Ms. Pinky Chaudhuri

MESSAGE:

Attached is Ms. Chaudhuri's resume.

As Josie Bassinette indicated to you previously, it would be appreciated if this could be handled by your office. Please copy your response to Ms. Bassinette and myself.

Thank you

Transmission authorized by: authorization

If you experience any problem in receiving this transmission, inform the sender at the telephone or fax no. listed above.



Record Removal Notice

File Title Michael Bruno's chronological correspondence - May-Dec 1995		Barcode No. 1459983		
Document Date 05/15/1995	Document Type Letter			
Correspondents / Participants From: Pinky Chaudhuri To: James D. Wolfensohn, President				
Subject / Title [Application]				
Exception(s) Personal Information				
Additional Comments		The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information or other disclosure policies of the World Bank Group. <table border="1"><tr><td>Withdrawn by Salma Berrada</td><td>Date April 29, 2025</td></tr></table>	Withdrawn by Salma Berrada	Date April 29, 2025
Withdrawn by Salma Berrada	Date April 29, 2025			

D

The World Bank
Washington, D.C. 20433
U.S.A.

MASOOD AHMED
Director
International Economics Department

October 12, 1995

Mr. Charles H. Dallara
Managing Director
The Institute of International Finance, Inc.
2000 Pennsylvania Avenue, N.W. Suite 8500
Washington, D.C. 20006-1812

Dear Charles,

I am writing in response to your September 28 letter to Mr. Wolfensohn, enclosing the report prepared by the IIF Working Group on "Improving Standards for Data Release by Emerging Market Economies." As you know, we share your view on the importance of comprehensive and timely data availability for emerging markets. Your initiative and that of the Fund will help developing countries prepare the kind of information needed by market participants.

In light of the increasing integration of developing countries into the global financial market, and the associated changing structure of external financial flows to these countries, we are actively exploring how to expand the coverage and improve the quality and timeliness of the data that the Bank makes available on emerging markets. The redesign, currently underway, of the Bank's Debtor Reporting System and of related statistical publications are part of this effort. We are also looking specifically at your suggestion on releasing individual country debt data as they are prepared during the course of the year.

In view of our common interests, I would welcome the opportunity to meet with you and members of the Working Group to discuss how the Bank can contribute to improved information on emerging markets.

Best regards,

A handwritten signature in black ink, appearing to be 'Masood Ahmed', with a long horizontal stroke extending to the right.

Masood Ahmed

bcc: Messrs. R. Frank (EXC), M. Bruno (DECVP)

cc: AB
PC
MP

Mr. Masood Ahmed

10/5

Masood

Michael would appreciate it
if IEC could respond to attached.
Could he please see your
response (in final) by cob 10/12.

Many thanks

Kate

att.

061

The World Bank

1818 H Street, N.W.
Washington, D.C. 20433, U.S.A.



With the compliments of
Richard Frank
Managing Director

95 OCT -5 AM 5:03

RECEIVED
DEVELOPMENT & ECONOMIC
POLICY

Mr. Brann -

Michael -

*This came to me - but I
believe DEC is working on the general
topic of Data from LDCs ? /Richard*

011
→ M A
95 OCT -5 AM 5:11
AB
PC
MP
the set up only
for this com.
10/6

CORRESPONDENCE MANAGEMENT FOR THE PRESIDENT'S OFFICE
CHORUS
External Correspondence Profile

Reference #. EXC-03389

For Action: Richard Frank VPU: EXC Room #: E-1227 Telephone: 30585	Log Date: 10/04/95 09:04:00 AM Status: Open Response Date:
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CORRESPONDENCE DESCRIPTION:

From: Mr. Charles H. Dallara, Managing Director, The Institute of International Finance, Inc., Washington, D.C.
To: Mr. Wolfensohn
Dated: 09/28/95
Topic: Report: "Improving Standards for Data Release by Emerging Market Economies"

ACTION INSTRUCTIONS:

Due Date: 10/13/95

4. Please review and advise.

SPECIAL INSTRUCTIONS:

None

INFORMATION COPIES:

Please return to: Maree Aniba, EXC, E1227, 84138
--

EXC 03389

THE INSTITUTE OF INTERNATIONAL FINANCE, INC.
2000 PENNSYLVANIA AVENUE, N.W. SUITE 8500
WASHINGTON, D.C. 20006-1812

Charles H. Dallara
Managing Director

September 28, 1995

Mr. James D. Wolfensohn
President
World Bank
1818 H Street, NW
Washington, DC 20433

Dear Mr. Wolfensohn,

Please find enclosed a copy of a report by the IIF Working Group on Data Standards entitled "Improving Standards for Data Release by Emerging Market Economies." The report was prepared by IIF staff and representatives from 26 private financial institutions involved in emerging markets finance. It also incorporates comments from officials in emerging market economies.

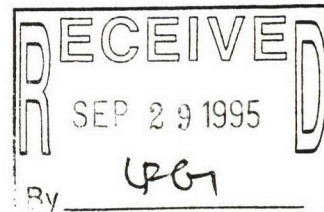
The report focuses mainly on the release of data by authorities in emerging economies. However, we also suggest that the public international financial institutions consider ways in which their own statistical publications might be improved. In particular, our members believe that it would be helpful if the World Bank worked toward more timely publication of its own comprehensive information on countries' external debt. One possibility might be to publish individual countries' statistics as soon as World Bank staff have compiled them rather than waiting until all countries' data are completed.

Best regards

Sincerely,

Charles

Enclosure



95 OCT -5 AM 5:11
SEP 28 1995
September 28, 1995

STANDARDS FOR DATA RELEASE BY EMERGING MARKET ECONOMIES

Report of the Institute of International Finance Working Group on Improved Data Provision by Emerging Economies

The growing integration of emerging economies into global capital markets and their efforts in recent years to reform their economic management have increased the need for improved economic data from the perspective of both domestic and international investors as well as policymakers. Many countries have already made significant progress in the provision of information. Others are seeking actively to improve their data. Some important gaps, however, remain, and the lack of transparency in emerging markets, together with the Mexican crisis, has reinforced the need to address these.

Assessment of countries' prospects, especially for external payments, depends substantially on their economic policies and underlying performance. Countries' ability to finance external payments will be influenced by international capital markets' perceptions and the scale of countries' existing external obligations.

Market participants, including creditors, investors, underwriters and traders, therefore, need comprehensive and timely information on emerging economies' policies, performance, and external liabilities. Improved data provision should also be helpful to policymakers in emerging economies. The Institute has formed a Working Group comprised of representatives of its members, including many of the leading private financial institutions doing business in emerging markets. This Working Group has developed, from a market perspective, a set of benchmarks for publication of data on the main economic and financial aggregates. A list of the benchmarks, together with our assessment of the extent to which countries are meeting them on average, is attached. We have also benefited from discussions with representatives of major emerging economies. A list of institutions represented on the Working Group is attached. The Institute puts forward these benchmarks as proposed standards for data release by emerging market authorities. We would encourage an effort by authorities to meet these standards, building on the progress already underway in many cases.

Improved data, of course, are no substitute for analysis. We would encourage all private investors and lenders to use the greater availability of more timely and comprehensive data to strengthen their analysis of risks in these markets. Better risk management, built on more

transparent markets, can contribute to greater discrimination by investors and reduce the prospects of unwarranted contagion effects between emerging markets.

It should also be noted that absence of data may not be evidence of poor economic performance. Some countries with relatively sound policies may not currently meet these standards, while others with weak performance may have better transparency. Availability of comprehensive, timely data, however, is likely to enhance markets' confidence in emerging economies and aid domestic authorities in implementing sound policies promptly.

The rest of this paper describes the benchmarks for fiscal and monetary policy indicators, economic performance data and information on external finance, debt and reserves. It also discusses the transmission of data to market participants and the role of the international financial institutions in improving data transparency.

1. Policy indicators

The Working Group and other analysts attach high importance to having good information on macroeconomic policies. Fiscal and monetary policies are powerful influences on demand, inflation and potential external imbalances. They need to be considered together because they may reinforce or offset each other. Their joint impact will influence interest rates, the exchange rate and the external balance of payments. Comprehensive and timely information on both budgetary and monetary developments, therefore, is essential for analysis of emerging economies' prospects.

(a) Public sector borrowing requirement

The thrust of fiscal policy and the impact of the public sector as a whole on the economy is measured best perhaps by the public sector borrowing requirement. This should cover not only the central government but also local and provincial authorities as well as the net borrowing of public enterprises. The latter need to include not only nonfinancial enterprises but also any quasi-fiscal operations of the central bank.

National practices vary widely for the collection of data on public sector activities. Representatives of several emerging economies, however, reported that discussion of programs with the IMF and technical assistance more generally from the international financial institutions had helped them refine public sector data. Policymakers themselves welcomed improved information. The Institute's members felt that while authorities should give priority to providing timely data on a national basis, they should also aim to move quickly towards internationally recognized standard presentations. This was particularly important for portfolio managers trying to compare data across countries. Public expenditure and revenue figures should be available as far as possible on the basis used in the IMF's *Government Finance Statistics*.

Particular problems can arise from the omission of "off-budget" categories such as social security and pension funds. Contingent liabilities in the form of guarantees, perhaps to support domestic financial institutions or enterprises, should also be reported wherever possible.

Few countries provide comprehensive and timely accounts for public sector activities, but because these are often the cause of subsequent economic imbalances and external payments problems, we attach considerable importance to improvements in this area. Authorities should aim to publish consolidated public sector accounts quarterly with a lag of not more than three months.

(b) Central government budget

Monthly or quarterly figures are available in some countries for central government revenues and expenditures, but often on a cash rather than an accruals or national accounts basis. This distinction is important where countries are running arrears. Seasonal factors can also often complicate interpretation of government revenues and expenditures. Authorities, however, should aim to publish figures monthly on both a cash and accruals basis.

Some emerging economies' officials reported governments' reluctance to publish comprehensive and timely information on public sector activities because of domestic political sensitivities. Such reticence is difficult to justify. Domestic electorates, business and financial markets have a legitimate interest in governments' fiscal performance, as have external creditors and investors.

(c) Domestic credit

Public sector borrowing needs to be considered alongside monetary policy. Contributions by the domestic banking system to financing public sector borrowing have a potentially powerful impact on liquidity. This in turn may fuel additional private spending and hence inflationary pressures. Increases in domestic credit to private borrowers, as well as acquisition of net foreign assets by the banking system, may also add to liquidity. These developments can only be analyzed adequately through timely publication of a comprehensive monetary survey, along the lines of the IMF's *International Financial Statistics*. Almost all countries provide data on the monetary survey, but fewer than one-half make this available within a month.

(d) Monetary aggregates

Monthly data on monetary aggregates are provided by most countries, but the lag is also often unacceptably long. Emerging economies' authorities reported difficulties in obtaining data from commercial banks, as well as problems with the quality and auditing of banks' accounts in some cases. Sample surveys of banks needed to be representative because the positions of large and small banks might differ. Countries in Central and Eastern Europe and the former Soviet Union faced particular difficulties in data collection because of the substantial structural changes in their banking systems. The international financial institutions were providing technical assistance to several countries.

Supervisors of banks may be able to play an important role in improving banks' accounting practices and the reporting of data more generally, although supervisory authorities are sometimes separate from central banks. Bank supervisors need the balance sheets of domestic deposit-taking institutions for regulatory and prudential purposes. Central banks also need this information for the management of monetary policy.

The target should be publication of consolidated monetary accounts monthly with a lag of not more than four weeks. These should include not only the main monetary aggregates but also the credit and external counterparts. We recognize that this target is ambitious, but we attach importance to it because monetary data can be particularly helpful in understanding short-term economic developments and external reserve flows. Some emerging economy officials expected that participants in their own domestic financial markets would press for improved data as these markets develop.

(e) Central bank operations

An important factor in understanding the link between fiscal policy, external reserve movements and changes in domestic liquidity is the role played by the central bank. Prompt publication of the central bank's balance sheet along with the monetary accounts should have a high priority. Less than one-half of major emerging economies publish their central banks' balance sheets promptly.

(f) Interest and exchange rates

Among key indicators of monetary conditions are interest rates and exchange rates. These are typically already available daily on the international screen services. Difficulties, however, can arise in obtaining representative rates, e.g., for short-term interest rates, whether for interbank transactions or Treasury bills. Regular publication of representative rates by the authorities would help analysts. Exchange rates, likewise, may vary from the daily quotes where parallel or multiple exchange regimes exist. Greater transparency on these rates should be an objective.

2. Measures of economic performance

Macroeconomic policies can contribute importantly to economic imbalances, reflecting essentially an excess of domestic demand over supply. This may spill into increased inflation, a tendency towards external trade deficit or a combination of the two in the absence of corrective policies. The Working Group felt that analysts needed comprehensive measures of the main expenditure and output categories to assess the prospects for external payments. They also needed timely data on inflation and external trade to judge the impact of excess demand pressures.

(a) Output

Authorities in about one-half of the major emerging economies produce national accounts output data on a quarterly basis with an average lag of approximately three months. This is broadly comparable with most G-10 industrial countries and should be a standard at which all major emerging economies should aim. Data for the individual sectors of the economy should be available to show the main contributors to growth and help identify potential bottlenecks. Officials from countries in Central and Eastern Europe and the Former Soviet Union suggested that the steep recorded output falls in recent years were probably overstated because growing private sector activity was not captured fully by current reporting systems. Other emerging economies also reported problems collecting data on the informal sector, although reforms to broaden the basis of taxation might improve information in this area.

(b) Expenditure

Data on national accounts by expenditure are not readily available with authorities in less than 40 percent of countries producing quarterly data. This should be improved. Better data would allow both policymakers and analysts to judge the extent to which changes in demand reflect private or public consumption, gross fixed investment, stockbuilding or the net external sector. Data on public consumption and investment are increasingly available from the fiscal accounts. Some countries gather information on investment either from surveys of companies or indirectly from statistics for output and imports of capital goods. Data on private consumption remain elusive, although officials in some emerging economies reported that they were preparing household surveys.

Some market participants would welcome early indicators of economic activity; for example, prompt data on industrial production and retail sales. Officials from emerging economies, however, cautioned against reading too much into such partial information.

(c) Inflation

Various measures of inflation are relevant for different purposes. The most widely used indicator tends to be consumer prices, although these measure not only demand pressures in the consumer goods market but also tax and, in some cases, interest rate changes. Monthly data on consumer prices are available for most countries with a relatively short lag of about two weeks. This should be a general standard. In countries where inflation is particularly rapid, more frequent collection of data may be appropriate.

Data on other measures of inflation would also be welcome. In particular, information on producer prices can give not only an early warning of future movements in consumer prices but can also indicate pressures on companies' profit margins. Data on wages and especially unit labor costs can also provide evidence of movements in competitiveness.

(d) External trade and current account

Information on external trade provides not only a further indicator of possible macroeconomic imbalances but also the likely need for external finance. Data are collected typically either through customs reporting or the record of foreign exchange transactions through the banking system. The former tends to align more closely with national accounts' concepts and is generally preferable to the foreign exchange record, which may be distorted by leads and lags in payments. Almost all emerging economies provide monthly trade data. Border trade, however, is not always recorded accurately, nor is trade in military equipment. Timeliness could also often be improved. Only one-half of the major emerging economies make trade data available on a timely basis. A maximum one-month lag should be the aim.

Information on trade flows should be expanded by publication of data on all current account transactions, including trade in services, interest payments and receipts, and transfers. In some emerging economies, these "invisible" flows form a substantial part of current payments. Almost all emerging economies publish current account data, but only about 60 percent provide the data with a lag of three months or less. This should be the benchmark.

3. External finance, debt and reserves

(a) Capital flows

Emerging economies' ability to finance their external payments is an essential indicator of creditworthiness. Assessment of this requires information on external capital flows. Data on these, however, are often both sparse and tardy. Few countries produce adequate data for disbursements and repayments by either borrower or creditor categories. Major efforts are needed. Data on capital flows should be collected in parallel with information on the stock of external debt. Data for flows and stocks should be reconciled where sources differ.

The target should be provision of quarterly data by both major borrower and creditor. Statistics need to distinguish between borrowing by the public sector, by domestic banks and by the rest of the private sector. Recent events in some major Latin American countries have shown the need to monitor carefully the external liabilities of the banking system. Borrowing by private companies is also increasing in importance as state enterprises are sold in many countries.

Borrowing also needs to be distinguished by instrument as capital markets develop and new forms of external finance are added to traditional loans from commercial banks and loans and guarantees by official agencies. In particular, markets need information not only on international securities issues by emerging economy borrowers but also nonresidents' purchases of domestic securities. Flows of both portfolio equity and direct investment also need to be captured fully. Transactions by residents, who have often provided an important share of inflows through capital repatriation to emerging economies, likewise need to be tracked. Reporting systems in emerging economies have often not kept pace with the changing pattern of capital flows in the balance of payments, and need to address these issues urgently.

(b) External debt and reserves

Information on capital flows should be supported and reconciled with data on external debt in the same quarterly time frame. This is a particularly demanding objective, but figures for the stock of external liabilities by the major categories of borrower -- public sector, domestic banks and other private borrowers -- may often be collected from balance sheets more easily than data on flows. Ideally the same sources should be used, which suggests the same quarterly time frame is appropriate, particularly where countries have substantial short-term obligations or active foreign participation in domestic capital markets. Data should show the breakdown by creditor, including the international financial institutions, creditor governments, foreign banks and other private lenders.

Data should also be available by instrument, including nonresidents' holdings of internationally issued bonds, domestic securities, commercial paper and deposits in domestic banks. Short-term liabilities should be a particular focus of attention. The currency composition should be available. In addition, countries need to publish any transformation of liabilities or any "off-balance sheet" obligations incurred as a result of derivatives transactions.

Published data on amortization are almost universally poor. This needs to be remedied with amortization figures for the next five years based on the latest debt stock figures and published on the same detailed basis by borrower, creditor and instrument. Short-term obligations should be available on a quarterly basis, particularly where these form a significant portion of total debt.

About two-thirds of major emerging economies provide data on the medium-term liabilities of public and private borrowers, together with short-term debt. Less than one-half of these, however, provide information in a timely fashion. Comprehensive and timely data on amortization due is even more elusive.

All major emerging economies provide information on their end-month external reserves, but publication is often tardy. Less than one-half make the data available in two weeks. This is difficult to explain since central banks should know their reserve position daily.

Officials in emerging economies pointed to the increased difficulties of obtaining information on capital flows and residents' external obligations as capital controls were relaxed. Several countries' authorities, however, still insist that private borrowings are registered. Others rely on data from transactions through the domestic banking system. Some are preparing surveys. Improved monitoring of nonresidents' holdings of domestic debt instruments may be helpful as local capital markets develop. Stock exchange authorities may be able to play a fuller role in gathering information on nonresidents' equity holdings.

Authorities in emerging economies should also monitor carefully the external financial transactions of residents, especially where substantial liquid domestic assets are available to be moved abroad, posing a potential draw on international reserves. Policies must be directed to reestablishing and then maintaining the confidence of both foreign investors and domestic residents -- particularly where past restrictions on external payments have left a legacy of distrust.

Actions to improve reporting in emerging economies may need to be supplemented by greater efforts to collect data directly from investors and creditors in industrial countries if an adequate picture of emerging economies' external liabilities and capital account transactions is to be obtained.

4. Transmission of data

We have adopted a flexible interpretation of data availability in our assessment of current practice, scoring data as being provided not only if it has been published but if it is readily available to analysts on request. This, however, may not necessarily meet the needs of capital market participants. The sensitivity of international capital markets to new information places a special onus on those emerging economies, whose obligations are traded on these markets, to provide data in both a regular and timely form. Dates and times for the release of key statistics should be announced in advance. Some emerging economies' authorities have already begun to release data electronically, and this practice should be followed more generally so that all market participants may have access simultaneously. Countries should also make data available in standard formats with tables and commentary in the languages of the major financial centers where their securities are traded.

5. Role of the international financial institutions

Officials from emerging economies praised the technical advice provided by the international financial institutions on improving the quality, collection methods and timeliness of data. Staff from these institutions, in particular, have helped country experts devise data methods that meet international standards. Emerging economy officials, however, suggested that technical assistance should be extended beyond short-term advisory missions to help with the implementation of new data systems, including staff training.

The international financial institutions, especially the IMF, have a potentially important role in promoting improved data standards in emerging economies -- both for their own surveillance of countries' performance and for dissemination to market participants. A key objective of IMF surveillance should be the promotion of market discipline through encouraging countries to release comprehensive and timely information. This would increase IMF leverage, help avoid crises and reduce the potential call on official financial support. The IMF might also consider playing an active role on behalf of the international financial community as a whole in auditing the availability, quality and timeliness of data provision at least by countries seeking access to global capital markets. This could require some reordering of the IMF's priorities and a special focus on countries' external financial situation.

The IMF should also seek to improve the timeliness of its own statistical publications, especially the monthly *International Financial Statistics*, bringing them more closely into line with the data already available in more dispersed form from national sources.

Efforts by the World Bank to speed publication of its own comprehensive information on emerging economies' external debt and by the Organisation for Economic Co-Operation and Development to improve its data on creditor governments' activities would also be helpful. The Bank for International Settlements might also consider the scope for reducing the lag in publication of banks' claims on emerging economies, and the Paris Club might usefully provide more details on rescheduling agreements, including interest capitalization and future repayments.

6. Conclusion

The Working Group concluded that inadequate or tardy information was likely to add to uncertainty and volatility in markets. It also complicated prudent macroeconomic management in emerging economies. A more transparent system for the regular and timely publication of comprehensive data on the key aspects of emerging economies' performance, policies and external position would help investors and creditors to base their analysis and decisions on up-to-date information. It could minimize the prospect of surprises when a country's economic performance deteriorates. Accordingly, it could be one element of a more sustainable approach to emerging markets finance. It would also provide domestic policymakers with better information to identify any problems early and take corrective action.

Analysis of the data provided by almost 30 major emerging economies shows that about two-thirds of major emerging economies provide information on at least 80 percent of the main economic indicators. This is an important aspect of transparency. Roughly one-fourth of the countries produce a significant amount of data in a timely fashion. None, however, currently

meets all our suggested criteria for both comprehensiveness and timeliness of the release of information, although the provision of data is improving rapidly in many countries.

The Institute has drawn attention to the gaps in information in discussion and correspondence with individual countries and with its members. We will continue to monitor improvements. To the extent feasible, we will be willing to work with authorities in advising them on steps needed to meet the standards. This will take countries time where new systems for data reporting are needed, but these issues should be addressed urgently. We expect to provide an assessment of the extent to which countries' provision of data meets the proposed standards by March 1996. Market participants may also wish to analyze directly the provision of data and countries' efforts to improve the flow of information. The international financial institutions, in their regular consultation with member governments, can help countries improve the provision of information. In some cases, technical assistance may be useful so that countries may benefit from best practice statistical and accounting techniques.

The main responsibility for improving the quality of data and releasing information promptly -- preferably electronically in internationally recognized format -- rests with emerging economies' authorities. Investors and creditors in these markets should be fully aware that improved data is only one element. This must be followed by rigorous analysis.

Data Availability Summary: Periodicity and Timeliness

September 1995

*Major Emerging Markets **

	Emerging Market Benchmark:		Emerging Market Performance:	
	<u>Periodicity</u>	<u>Lag</u>	<u>% Reporting on Variable</u>	<u>% Timely on Variable</u>
<u>National accounts</u>				
Output	Q	12	100.0	55.6
Expenditure	Q	12	92.6	37.0
<u>Inflation</u>				
Consumer prices	M	2	100.0	81.5
<u>Balance of payments</u>				
Exports and imports	M	4	100.0	48.1
Current account	Q	12	100.0	63.0
Capital account	Q	12	96.3	63.0
<u>External assets and debt</u>				
Reserves	M	2	100.0	44.4
Public borrowers	Q	12	81.5	40.7
Private borrowers	Q	12	63.0	37.0
Short-term	Q	12	66.7	37.0
Amortization	Q	12	48.1	18.5
<u>Monetary accounts</u>				
Monetary survey	M	4	92.6	33.3
Money supply	M	4	100.0	51.9
Domestic credit	M	4	100.0	37.0
Central bank balance sheet	M	4	96.3	44.4
Interest rates	W	1	92.6	74.1
Exchange rates	D	0	100.0	100.0
<u>Fiscal accounts</u>				
Central government budget	M	4	100.0	33.3
Public sector borrowing	Q	12	59.3	22.2

Q = quarterly, M = monthly, W = weekly, D = Daily

Lags are in number of weeks between end of period and availability of data.

* Argentina, Brazil, Chile, China, Colombia, Czech Republic, Greece, Hungary, India, Indonesia, Israel, Kuwait, Malaysia, Mexico, Morocco, Peru, Philippines, Poland, Russia, Saudi Arabia, South Africa, South Korea, Taiwan, Thailand, Tunisia, Turkey, Venezuela

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WORKING GROUP OF THE INSTITUTE OF INTERNATIONAL FINANCE
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Banco Santander de Negocios

Bankers Trust

Bank Brussels Lambert

Bank of Tokyo

Barclays Bank

Bayerische Vereinsbank

Chase Manhattan Bank

Commerzbank

CS First Boston

Dresdner Bank

Generale de Banque

HSBC Holdings Plc

J.P. Morgan

Lloyds Bank Plc

Monte dei Paschi di Siena

Norddeutsche Landesbank Girozentrale

Republic National Bank of New York

Royal Bank of Canada

Royal Bank of Scotland Plc

Sakura Bank

Standard Bank London Limited

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The World Bank

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September 15, 1995

Ms. Sakiko Fukuda-Parr
Director
Human Development Report Office, UNDP
336 East 45th Street
New York, NY 10017, USA

Dear Ms. Fukuda-Parr:

This is in response to your letter of August 8 addressed to Mr. Wolfensohn.

Thank you for seeking collaboration from the World Bank in the preparation of the Human Development Report 1996. We appreciate the opportunity to work with the UNDP on this important report, and we are especially pleased that you have selected as the theme of the Report the relationship between human development and economic growth. Much of the proposed content of the Report is closely related to the work undertaken at the Bank.

We would like to provide you with as useful a contribution to the 1996 Report as possible. I understand that collaborative efforts have been underway for some time, starting at your meeting with Mr. Michael Bruno and his team where preliminary ideas were discussed for the Report's outline. In the weeks and months ahead, we would like to encourage continued consultations between the UNDP team working on the Report and Bank staff. Mr. Lyn Squire, Director of the Policy Research Department, and Mr. David de Ferranti, Director of the Human Development Department, could serve as the contacts for such a purpose.

As a launching point for our contribution, we are enclosing for you a select number of publications which we feel might be particularly useful in the preparation of the Report. They are:

Poverty, Inequality and Growth
Advancing Social Development
Building Human Capital for Better Lives
Population and Development
Priorities and Strategies for Education
Investing in Young Children

A New Agenda for Women's Health and Nutrition
Equity and Growth in Developing Countries: Old and
New Perspectives on the Policy Issues

Please consider this package of materials a starting point from which further consultations can occur.

As part of its regular work, the World Bank prepares a number of publications which might be of interest to your team working on the Report. We have included a list of recent publications on both general and specific topics, as well as some country profiles. Should you or your team wish to consult these or other publications, please contact us and we will forward them to you. Additionally, the Bank has a database of social and economic statistics relevant to the Report available on the Bank's WorldWideWeb site.

Regarding your proposed outline for the Report, we are enclosing some specific comments in an attachment to this letter. The Report, we believe, appears to be well balanced, both on the topics addressed and the countries selected. One particular issue of interest to us is that the link between human development and economic growth be addressed in a two-directional way.

Please rest assured that we stand ready to continue with more collaboration with the UNDP on this important undertaking.

Sincerely,



Myrna Alexander
Acting Vice President
Human Capital Development and Operations Policy

Attachments

cc: Mr. James D. Wolfensohn, President

**Comments on the
Consolidated Draft Outline of the
Human Development Report 1996**

The following comments are offered as an initial response to the UNDP's request for collaboration with the World Bank on the Human Development Report 1996.

The Report has a clear focus on the relationship between human development and economic growth. We feel it is important that the analysis of this relationship flow from chapter to chapter, and this seems to be well laid out in the outline.

One area of the Report which may benefit from further consideration is how Chapter 4, which gives an overview of country experience, can fit neatly into the flow of the document. It would also be useful if the Report elaborates on the criteria used in selecting the countries to be examined in Chapter 4. It is possible that significant differences in the demographics of the countries may have the effect of distorting any aggregate indicators.

In our opinion, the Report might also benefit from a discussion of some broad sociopolitical measures of human welfare, such as measures of political rights, rule of law, rights of women, etc. This discussion could include an analysis of the relationship between these measures and economic growth.

How the Report can address income mobility is another relevant topic, and we would like to encourage a full discussion on this subject as well.

The discussion of the effects of economic growth on human development might also benefit from including a discussion of the associated processes including the effects of growth in generating additional resources for investment in health, education and other key components of human development. In this context, income distribution and poverty then condition how effectively growth is likely to impact on human development.

In our opinion, the relationship between human development and economic growth needs a careful assessment of how the interaction occurs in both directions. Moreover, we believe it would be useful for the purpose of policy formulation to make a distinction between whether the break down in the relationship occurs in the link from human development to economic growth or in the link from economic growth to human development, or possibly in both. This distinction in your analysis might prove useful when considering the impact on economic growth of investments in human development. We think that one key issue may revolve around the trade-offs a government can face between investments in human development that clearly promote economic growth and those that address a lack of investment by the private sector.

**List of Relevant World Bank Publications
for the Human Development Report 1996**

Adjustment in Africa: Lessons from Country Case Studies. Edited by Ishrat Husain and Rashid Faruquee. A World Bank Regional and Sectoral Study. 1994.

Better Health in Africa: Experience and Lessons Learned. Development in Practice Series. 1994.

Higher Education: The Lessons of Experience. Development in Practice Series. 1994.

Malnutrition in Cote d'Ivoire: Prevalence and Determinants. David E. Sahn. Social Dimensions of Adjustment in Sub-Saharan Africa Working Paper No. 4. 1990.

Measuring the Impact of Fatal Adult Illness in Sub-Saharan Africa: An Annotated Household Questionnaire. Martha Ainsworth et. al. Living Standards Measurement Study Working Paper No. 90. 1992.

National Policies and Economic Growth. William Easterly. Journal of Monetary Economics. 1993.

Political Economy of Poverty, Equity, and Growth: Brazil and Mexico. Angus Maddison and associates. Oxford University Press. 1992.

Political Economy of Poverty, Equity, and Growth: Costa Rica and Uruguay. Edited by Simon Rottenberg. Comparative Study. 1993.

Political Economy of Poverty, Equity, and Growth: Five Small Open Economies. Ronald Findlay and Stanislaw Wellisz. Comparative Study. 1993.

Political Economy of Poverty, Equity, and Growth: Sri Lanka and Malaysia. Henry J. Bruton. Oxford University Press. 1992.

Population and Income Change: Recent Evidence. Allen C. Kelley and Robert M. Schmidt. Discussion Paper No. 249. 1994.

Primary Education. A World Bank Policy Paper. 1990.

cc. Messrs./Mmes. Aniba (EXC); Bruno, Baird, Vieira Da Cunha (DECVP); Squire, Best (PRDDR); Jimenez, Ravallion, Pritchett, King, Longo (PRDPH); Easterly (PRDMG); Husain, Demery (PSP); Choksi, Psacharopoulos (HCOVP); Boucher (OPRNY); Raphaeli (OPRPG); de Ferranti, Barrientos, Saxenian (HDD); IISC.

EXC-02619

HCO#0067

Human Development Department
N:\STAFF\WALKER\UNDP.DOC
September 15, 1995 5:22 PM

J.W. Chon

August 23, 1995

Mr. Yekutiel X. Federmann
P.O. Box 3219
Tel Aviv 61031
Israel

Dear Mr. Federmann:

I am responding to your letter of July 31, addressed to Dr. Hans Tietmeyer, President Deutsche Bundesbank, and copied to Mr. James Wolfensohn.

You have, of course, raised an important issue regarding the stability of currencies. Although this is not a primary area of responsibility for the World Bank, I assure you that we monitor developments carefully and will continue to interact with other interested parties, including our sister institution, the International Monetary Fund, that has more direct responsibility for the issues you have raised.

Yours sincerely,



Mark Baird
Acting Vice President
Development Economics

THE WORLD BANK GROUP
Office of the Vice President & Chief Economist
Development Economics Department

ROUTING SLIP		DATE: August 23, 1995	
NAME			ROOM. NO.
Mr. Lyn Squire, Director, PRD			N11-051
cc: Mark Baird			
	URGENT		PER YOUR REQUEST
	FOR COMMENT		PER OUR CONVERSATION
	FOR ACTION		NOTE AND FILE
	FOR APPROVAL/CLEARANCE		FOR INFORMATION
	FOR SIGNATURE		PREPARE REPLY
	NOTE AND CIRCULATE		NOTE AND RETURN
RE: Attached			
REMARKS: Lyn, Mark suggest that you may want to ask someone in the Macro Division to prepare a brief response/acknowledgment to Mr. Federmann. We have been asked to respond by August 25th. It could go from Mark as acting V.P. May thanks. Kate			
FROM Kate Oram		ROOM NO. N6-045	EXTENSION 31107

Correspondence Management for the President's Office
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External Correspondence Profile

Reference #: EXC-01907

For Action: Michael Bruno
VPU: Room #: Telephone:

Log Date: 08/18/95
Status: Open
Response Date:

Correspondence Description:

From: Yekutiel X. Federmann
To: Mr. Wolfensohn
Dated: 07/31/95
Topic: unstable currencies

Action Instructions

Due Date: 08/25/95

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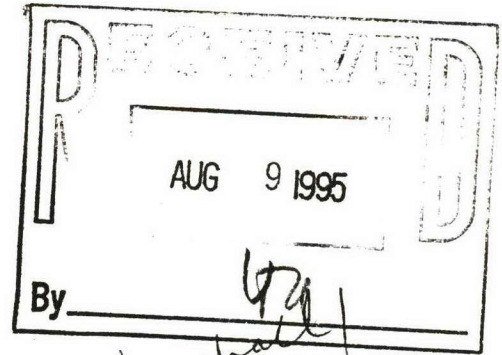
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EXCJ907

WITH COMPLIMENTS

OF YEKUTIEL X. FEDERMANN

MR. JAMES WOLFENSOHN,



D-60431 Frankfurt a. Main.

Fax: 00-49-69-5604242

Dear Dr. Tietmeyer,

I am hesitating for some time now if I should write to you on a subject we touched in our last meeting in your office in Frankfurt, namely Stability of Currencies.

After reading the attached article in the International Herald Tribune I take the liberty of addressing you knowing that you are an expert, mature in experience and open to new thoughts and thinking.

As an industrialist I have learnt the hard way that unstable currencies, and this refers mainly to the Dollar and the German Mark, are a negative and dangerous factor for the stability of industry and trade and a danger to expansion of industry which is so much needed all over the world.

I believe that the fluctuations in the currency markets, are not only creating nervousness, but economic threats and dangers for industry and trade worldwide. They could lead to inflation in one corner of the world and devaluation in another.

I cannot absorb in my production programme that suddenly raw materials based on European currencies such as chemicals or textiles, machinery or spare parts will become 7 - 10% more expensive because my Dollar value vis-a-vis the European currencies has gone down (see the Japanese economy). Currencies must be stable; prices of commodities and services can rise or decline.

In the United States economy this problem is of hardly any importance as America is a continent, rich in raw materials, production and capacity. It is like an old British gold Sovereign, or the Maria Theresienthaler - domestically stable. Only a change of social conditions in the States, such as domestic strikes, unemployment, unrest or national disaster, may have influence on the price level in the States, but not on the Dollar as a currency.

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& OPPORTUNITIES

J. W. Chron

Mr. Naresh Kumar
National Institute of Science, Technology
and Development Studies
Dr. K.S. Krishnan Road
Pusa, New Delhi - 110012
India

Dear Mr. Kumar:

I am writing in response to your letter of May 18, 1995, addressed to the President of the World Bank, which was accompanied by a research proposal, "Model Dynamics of Growth in the Third World."

Your research proposal indicates that you wish to carry out a critical evaluation of models of technological and economic change. In this area, the research returns are greater from addressing the empirical and behavioral premises that underlie the models than on producing additional surveys of the models themselves.

For example, many global models place relatively strong restrictions on the degree to which inputs can be substituted for each other in production processes. The global 'optimists' assert that substitution will be relatively easy, and the global 'pessimists' assert that substitution will be limited and difficult. Empirical work on critical issues such as this appears to have a higher priority than reviews.

I must also inform you, however, that individual research projects supported by the World Bank are components of Bank departmental work programs, are closely integrated with the Bank's operations, and involve Bank staff. The Bank does not fund individual external research projects such as the one you have sent.

Bank support for research carried out external to the Bank is usually for technical research that is funded on a programmatic, as opposed to a project, basis. For example, the Bank supports the Consultative Group for International Agricultural Research which operates numerous international research centers which carry out research designed to increase the yields of crops and livestock.

Yours sincerely,



Gregory K. Ingram,
Administrator,
Research Advisory Staff

bcc: EXC
Michael Bruno

Greg

JUN 2 1995

THE WORLD BANK GROUP

ROUTING SLIP		DATE: June 2, 1995	
NAME		RECEIVED	
Mr. Greg Ingram		ROOM. NO. N9-033	
JUN 02 1995			
RESEARCH ADVISORY STAFF			
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☐	FOR COMMENT	☐	PER OUR CONVERSATION
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RE: Attached			
REMARKS:			
Greg, Could you please handle and copy to Michael and EXC. Thanks. Kate Deadline 6/6; don't know why they've given us such a tight deadline on this.			
FROM Kate Oram		ROOM NO. S9-035	EXTENSION 31107

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Server error: Entry not found in index

Date: 05/30/95
Status: Open

Correspondence Description:

From: Naresh Kumar, New Delhi, India
To: Mr. Wolfensohn
Dated: 05/18/95
Topic: Research proposal "Dynamics of Growth in the Third World"

Action Instructions

Due Date: 06/06/95

Please handle/respond on behalf of Mr. Wolfensohn and provide a copy to EXC

Special Instructions

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NISTADS

डा० के० एस० कृष्णन् मार्ग, पूसा, नई दिल्ली-११००१२ (भारत)

NATIONAL INSTITUTE OF SCIENCE, TECHNOLOGY AND DEVELOPMENT STUDIES
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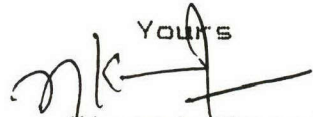
Naresh Kumar
'Scientist'

Dated:
18.05.95

No: NISTADS/TS/95

Sir,

National Institute of Science Technology & Development Studies, New Delhi is a pioneer national research institution under the aegis of Council of Scientific & Industrial Research. I am sending herewith a research proposal entitled '**DYNAMICS OF GROWTH IN THE THIRD WORLD**' for your kind consideration & perusal. I want to under take this study. As the whole world is facing an acute problem of economic crisis, I hope the outcomes of this study would be beneficial for both the developing & developed countries. Therefore, I am writing you to sponsor this project. Your early response will be highly appreciated.
Thanks with regards.

Yours

(Naresh Kumar)

Enc: Research proposal.

To,
The President
The World Bank
1818 H. Street, N.Y.
Washington D.C., 20433
USA

Model Dynamics of Growth in the Third World

=====

NARESH KUMAR

National Institute of Science
Technology & Development Studies
Dr. K.S. Krishnan Marg, Pusa,
New Delhi-110012 (INDIA)

Introduction

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The purpose of the study is to present a critical evaluation of models of technological and economical change. This is intended primarily as an integrative work that will bring together the pertinent models of techno-economic change in the developing countries. Technological change is a dynamic and multidimensional phenomenon involving invention, innovation, transfer and diffusion of technology. It is taken for granted by society that technological change is a harbinger of economic development (1). The manifestation of technological change may be the development of new products and machines and better and easier ways of doing things and solving problems. Interest in technological change and economic development is not only intense in the developed countries but also in the developing world. Thus, it will bring together the models and theories of technoeconomic change to facilitate comparative and interdisciplinary research and study of technology in general and technological change in particular without being constrained by disciplinary constraints and loyalties.

Literature Review

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Looking back at the history of future studies, the 1970s can be described as the decade of Global Modelling. These models are witnessed that there is a need for a new international economic order. This led to an impressive number of publications which are often called "Global Models". In particular, under the auspices of the Club of Rome- which has been an important stimulator of this project - a number of famous futures studies appeared, such as Limits to Growth by Meadows (2), Mankind at the Turning point by Mesarovic and Pestel (3), and Reshaping the International Order (RIO) by Jan Tinbergen (4). A Latin American Model, published as New-Society by the Argentinian bariloche Foundation (5).

Other important model studies of that decade were Leontief's The Future of the World Economy (6), Kahn's The Next 200 years (7) and his World Economic Development (8), the OECD study Facing the Future (9) and the books of the World Order Models Project (WOMP), of which Falk's A Study of Future Worlds (10), Galtung's The True World's (11), and Mendlovitz's On the Creation of Just World Order (12), are the most well known. In short, these studies had in common a long-term and global perspective with bold, creative, challenging and encompassing on the future of the plant. Moreover, they were based on the hope and expectations that these models could make a contribution to the solution of global problems. In that sense these models were explicitly policy oriented. On the other hand, these studies were also a reflection of the two most burning global problems of that decade- the perceived need for a new international economic order to change the North-South relationship by decreasing the gap between the rich and the poor nations, second, what has become known as "the global problematique", by which is meant the combined problems of non-renewable resources depletion, environmental deterioration, overpopulation and pollution which threaten the survival of human kind.

For many economists, models are associated with a mathematical representation of reality, and for them global modelling is a new field made possible by invention of advanced computers which based on the new technique of system analysis. What is meant here is something different. A model is seen here

as a way of grasping the essence of the complex reality by what the German sociologist Niklas Luhmann has called the "Reduction of Complexity" (13). This can be done in a quantitative way but also in a qualitative way. Thus, model dynamics in this context stands for the new mood of time in the scientific realm with deep concern for the burning problems of our time like the poverty gap between the North and the South and the ecological problematique.

After the 1970's, the golden age of global modelling seemed to be over, for during the 1980s, there was little action on this front, albeit with an emphasis on mathematical models. By 'global' is meant here an encompassing view on either the globe in totality or on a continent or region, if the relationship with rest of the globe is emphasized. In brief it can be said global models are characterized by a long-term perspective, and more than one model is generally presented, often in the form of a scenario (14). It is difficult to identify the exact reasons for this decline of political global models and of the global models movement. One could argue that the decline was an outcome of frustration, since the influence of these models was less than expected and hoped for. Another explanation for this decline is a change in the overall "mood of the time" (15).

In the UN discussion about global development, the world of global institution can be divided into three systems:

- first system consists of governments and intergovernment organizations.
- second system consists of business world and especially the transnational corporations.
- third system is represented by people acting collectively through social movements, voluntary institutions and association.

First system is described as old model, which was seen as the main 'shaping factor' for global reform. Second system may

be defined as the new models. This shift is not only visible in reshaping Europe, but also in studies which are carried out by governmental agencies. To give an example, in the European Challenges Post-1992, a report from an EC think tank (16), which deals with shaping factors and shaping actors. The views of the business community are given more prominence than the views of national governments.

Future Scope

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With the new front stage role of the second systems it is not surprising that a new ideology emerges, which states that sustainability and high economic growth go hand in hand, or, to put it even stronger, that high economic growth is a pre-requisite for a sustainable society. The argument for this high economic growth is that is necessary in order to 'Clean-up the mess' created by our environmentally unfriendly behavior, only when industry grows and companies make good profit, we are within to invest in environmental measures. In this context developing countries may be mentioned, where the environmental deterioration and resources exploitation is much worse than in developed countries, because of the backwardness of the means of production in that region. The reason is simple-with good profit, based on a high level of economic growth, industry will be much more willing to invest in environmental measures; different form of 'ecotax' will be more financial room for technological innovation. The general idea behind this is that business has to do the job and role of government is limited.

It is interesting that recent study Beyond the Limits (17) of the Meadows couple try to maintain that there is little room for optimism with regard to the global problematique. Contrary to most other recent models, the Meadows keep emphasizing the necessasity to restructure the system. In his different models Meadows argues that to avoid collapse in economy we have to start restructure our economy today with the level of technological optimism and with the time perspective.

It is concluded that in some respects there is progress, in particular in the scientific realm. Scanning the Future (StF) is explicitly based on economic theories, and that is rather exceptional since most models, and certainly the old ones, are rather poor in this respect, on the other hand these new models make a rather 'Cold impression', as they do not reflect a deep concern for the burning issues of our time. The problems of the poor nations are almost completely absent and the ecological problematique is presented within an optimistic framework. Thus in the whole scenario the ideology of the second system is dominated everywhere. These are the decisive actors in the economy.

Nobody seems to have taken into account that India, because of its recent change in economic policy or even more problemable, China, with its extremely high level of economic growth, may become the fourth and fifth economic superpowers in the foreseeable future. India is the largest emerging market in the world even though India is economically backward. Thus, in the age of free market or competitiveness there is a need to study the dynamics of economy of the Third World or to develop a model for sustainability of techno-economic of the developing countries. This will conclude who will win the economic cat-race, the USA, Japan, Western Europe or the developing countries would become economic giant.

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oder sozial technologie (Frankfurt, Suhrkamp, 1971)
14. Steenbergen, B.V., Global Modelling in the 1990s. Futures
Vol. 26(1) 1994, 44-56.
15. Steenbergen, B.V., Op Cit, reference 15.
16. Jacquemin and wright, Lignes d'horizon (Paris, Artheme
Fayard, 1990).
17. Central Planning Bureau, Scanning the Future, A long term
Scenario Study of the World Economy 1990-2015 (The Hague,
SDU Publishers, (1992).

L

M

JAMES D. WOLFENSOHN
President

95 SEP -7 PM 4:35

RECEIVED
DEVELOPMENT ECONOMICS
V.P. & CHIEF ECONOMIST

August 25, 1995

Mr. Isamu Miyazaki
Secretary General
InterAction Council
Akasaka Prince Hotel
Kioi-cho, Chiyoda-ku
Tokyo 102, Japan

Dear Mr. Miyazaki:

Thank you for your letter of July 21, 1995. I am most grateful to you for sharing with us the main documents arising out of the May 1995 meeting of the InterAction Council. We have reviewed these documents, and it is not surprising that out of such an eminent gathering should emerge such visionary ideas. I am indeed sorry that the Council has lost an important voice with the sad demise of Prime Minister Fukuda. I am sharing these papers with my colleagues so they may benefit from the experience and wisdom the Council brings to bear on a wide range of issues critical to the future of this planet.

I have three observations on the Council's deliberations. First, I fully share the emphasis placed in your discussion and in Malcolm Fraser's paper on the urgent need to curb population growth in the developing world. As you are aware, the Bank has been an active player in this field. We at the Bank fully share the emphasis the Council places on the critical role of education and women's status in reducing fertility. Over \$5 billion of the Bank's current annual lending is devoted to improving the status of women in primary health, education, population, nutrition and production. I will be traveling shortly to attend the Women's Conference in Beijing and will use that opportunity to put forward my ideas on how we propose to further improve the Bank's record in this area.

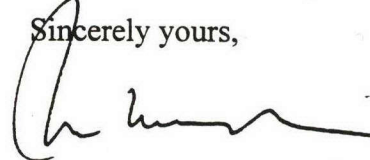
Second, I strongly support the Council's call for improved collaboration between the multilateral institutions. His Excellency, Andries van Agt's paper has some very useful ideas in this area. I attach a great deal of importance to building further on the effective collaboration that already exists between the World Bank and its sister institutions, the IMF and the WTO. I also see the Bank as a key player within the UN family, and intend to take our role in the UN system very seriously during my tenure at the Bank.

August 25, 1995

Third, His Excellency, Kurt Furgler's paper on global capital markets raises a number of issues of relevance for the World Bank. I agree with him that globalization of capital markets will bring important benefits to developing countries, but that it can also increase the costs of policy failures. Given the growing importance of private capital flows, we are undertaking a special study to better understand the changing nature of global capital markets and its implications for developing countries. We will continue to support our member countries in undertaking reforms so that they can exploit the opportunities created by increasing financial integration, and aim to improve further the flow of information on developing country markets. Finally, I would like to strongly endorse the point made by Mr. Furgler that improved access to private flows does not diminish the need for official support for the poorest countries.

best best with,

Sincerely yours,



James D. Wolfensohn

bcc: Messrs. A. Choksi, M. Bruno, M. Malloch-Brown, M. Ahmed

S. Lateef/A. Bhattacharya
EXC1941

THE WORLD BANK GROUP
Office of the Vice President & Chief Economist
Development Economics Department

ROUTING SLIP		DATE: August 23, 1995	
NAME			ROOM. NO.
Ms. Shaida Badiee, Acting Director, IEC			
cc: Mark Baird			
	URGENT		PER YOUR REQUEST
	FOR COMMENT		PER OUR CONVERSATION
	FOR ACTION		NOTE AND FILE
	FOR APPROVAL/CLEARANCE		FOR INFORMATION
	FOR SIGNATURE		PREPARE REPLY
	NOTE AND CIRCULATE		NOTE AND RETURN
RE: Attached correspondence to Mr. Wolfensohn			
REMARKS: Shaida, Could IEC (Sarwar?) prepare a quick, brief response to items 4 and 5 on attached, for Mr. Wolfensohn's signature. Please note that the due date is Friday, August 25th. Many thanks. Kate			
FROM Kate Oram		ROOM NO. N6-045	EXTENSION 31107

Correspondence Management for the President's Office
CHORUS
External Correspondence Profile

Reference #: EXC-01941

For Action: Michael Bruno
VPU: Room #: Telephone:

59035

Log Date: 08/18/95
Status: Open
Response Date:

Correspondence Description:

From: Isamu Miyazaki, Sec-Gen, interaction council
To: Mr. Wolfensohn
Dated: 07/21/95
Topic: sending info from 13th session

Action Instructions

Due Date: 08/25/95

3. Please prepare a response for Mr. Wolfensohn's signature.

Then please send the copy of the letter for Mr. Wolfensohn's signature back to Maree in E1227 together with the copy of the Log Sheet and incoming letter. In addition, please enclose two copies of the response letter which show the bccs, drafter's ID and EXC log number. These copies will be stamped " (signed) JAMES D. WOLFENSOHN ". Once the letter is signed, Ms. Kathy Ray will call your office. You can pick up the signed letter together with one "stamped" copy showing the bccs from D12069. VP Units are responsible for distribution of the original signed letter and the copies.

Special Instructions

Please see attached comments from Mr. Wolfensohn

Information Copies:

Please return to:
Maree Aniba, EXC, E1227, 84138

95 AUG 21 AM 11:18
RECEIVED
DEVELOPMENT ECONOMICS
VP & CHIEF ECONOMIST

8/22
Maree,
Should this
go to Choksi?
Thanks
Kate



INTERACTION COUNCIL

Helmut Schmidt, *Chairman*
 Federal Republic of Germany
 Takeo Fukuda, *Honorary Chairman*
 Japan
 Andries van Agt
 Netherlands
 Raul Alfonsin
 Argentina
 Giulio Andreotti
 Italy
 Corazon C. Aquino
 Philippines
 Oscar Arias Sanchez
 Costa Rica
 Lord Callaghan of Cardiff
 United Kingdom
 Miguel de la Madrid Hurtado
 Mexico
 Malcolm Fraser
 Australia
 Kurt Furgler
 Switzerland
 Valery Giscard d'Estaing
 France
 Mikhail S. Gorbachev
 Russia
 Selim Hoss
 Lebanon
 Kenneth Kaunda
 Zambia
 Lee Kuan Yew
 Singapore
 Tadeusz Mazowiecki
 Poland
 Olusegun Obasanjo
 Nigeria
 Misael Pastrana Borrero
 Colombia
 Shimon Peres
 Israel
 Maria de Lourdes Pintasilgo
 Portugal
 Roh Tae Woo
 Republic of Korea
 Jose Sarney
 Brazil
 Kalevi Sorsa
 Finland
 Pierre Elliott Trudeau
 Canada
 Ola Ullsten
 Sweden
 George Vassiliou
 Cyprus

Akasaka Prince Hotel
 Kioi-cho, Chiyoda-ku
 Tokyo 102, Japan

21 July 1995

Excellency:

The 13th Session of the InterAction Council (of former Heads of State and Government) was held from May 23 to May 26, 1995 in Tokyo, Japan.

No final statement was issued this year. Instead, the leadership of the Council decided to circulate the enclosed set of documents for your reference. Also

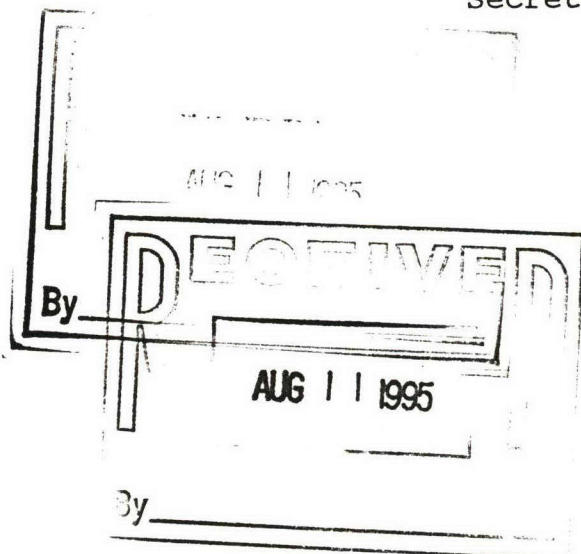
enclosed is a list of participants and a summary of the major points emerging out of the 13th Session.

The late Prime Minister Takeo Fukuda of Japan, the Founder of the InterAction Council, intended to mail the enclosed to you. Due to his sudden departure earlier in the month, this cover letter does not bear his signature, but this in fact was the final message from him. It is hoped that the documents will be studied carefully by your staff.

Yours Sincerely,

Isamu Miyazaki

Isamu Miyazaki
 Secretary-General





CONFIRMED PARTICIPANTS IN THE 13TH SESSION

Members

- | | | |
|--------------------------------|--|--------------------------|
| 1. Takeo Fukuda | Prime Minister of Japan
1976-1979 | <i>Honorary Chairman</i> |
| 2. Helmut Schmidt | Chancellor of the Federal Republic of Germany
1974-1982 | <i>Chairman</i> |
| 3. Pierre Elliott Trudeau | Prime Minister of Canada
1968-1979 and 1980-1984 | <i>Acting Chairman</i> |
| 4. Andries van Agt | Prime Minister of the Netherlands
1976-1979 | |
| 5. Oscar Arias Sanchez | President of Costa Rica
1986-1990 | |
| 6. Lord Callaghan of Cardiff | Prime Minister of the United Kingdom
1976-1979 | |
| 7. Miguel de la Madrid Hurtado | President of Mexico
1982-1988 | |
| 8. Malcolm Fraser | Prime Minister of Australia
1975-1983 | |
| 9. Kurt Furgler | President of the Swiss Confederation
1977, 1981, 1985 | |
| 10. Kenneth David Kaunda | President of Zambia
1964-1991 | |
| 11. Misael Pastrana Borrero | President of Colombia
1970-1974 | |
| 12. Roh Tae Woo | President of Republic of Korea
1988-1993 | |
| 13. Jose Sarney | President of Brazil
1985-1990 | |
| 14. Kalevi Sorsa | Prime Minister of Finland
1972-1975, 1977-1979, 1982-1987 | |
| 15. Ola Ullsten | Prime Minister of Sweden
1978-1979 | |
| 16. George Vassiliou | President of Cyprus
1988-1993 | |



INTERACTION
COUNCIL

Special Representative of Takeo Fukuda

Isamu Miyazaki

Chairman, Daiwa Institute of Research

Special Guests

Lester Brown

President, the Worldwatch Institute

Karen Brutens

Advisor to the President, the Gorbachev Foundation

Heitor Gurgulino de Souza

Rector, United Nations University

Huang Hua

Former Foreign Minister of China

Emile van Lennep

Former Secretary-General, OECD

Robert S. McNamara

Former President, the World Bank

Kiichi Miyazawa

Former Prime Minister of Japan

Petr Pithart

Former Prime Minister of Czechoslovakia

Nafis Sadik

Executive Director, United Nations Population Fund

Shin Hyon-Hwak

Former Prime Minister of Korea

Noboru Takeshita

Former Prime Minister of Japan

Cesar E. A. Virata

Former Prime Minister of the Philippines

Invited Journalists

Young-Hie Kim

Korea

Urban C. Lehner

U. S. A.

Flora Lewis

U. S. A.

Matthias Nass

Germany



INTERACTION
COUNCIL

MAJOR POINTS OF DISCUSSION AT THE 13TH SESSION OF THE INTERACTION COUNCIL

May 23-26, 1995
Tokyo, Japan

1. Although the world at large can avoid a food crisis until around 2020, the serious food shortage in developing countries, particularly in Sub-Sahara Africa, will become aggravated. It is essential to curtail population growth in these countries to cope with the situation. The world population quadrupled during this century to 5.8 billion and continues to grow by 90 million annually, with 95 percent of this growth coming in developing countries. Without controlling the population increase, it will be impossible to achieve food security, upgrading of living standards or arresting of environmental degradation. One recommendation is to make reduction in military spending and implementation of effective family planning programs in recipient countries a condition for receiving economic development aid. At present, official development aid remains at average 0.3 percent of donor countries' GNP. Since such aid is on a declining trend, more needs to be done than merely advocate its increase. It is essential to disseminate education more broadly to include girls and to upgrade the status of women as an essential condition to effective family planning programs. Moreover, the industrialized countries, which continue to destroy the ecological system through their excessive consumption must change their life styles and endeavor to reduce emissions of pollutants.
2. In reviewing multilateral institutions, mutual cooperation, mutual adjustment of activities and clarification of the division of labor are required. Coordination between the World Bank and the International Monetary Fund, and between those institutions and the Organization of Economic Cooperation and Development, the World Trade Organization and regional development banks needs to be improved. Some kind of a coordinating mechanism is necessary, embracing aid institutions and other U. N. agencies.
3. As for the United Nations itself, a review should be made concerning the composition of the Security Council, with the objective of making its role more appropriate to the post-Cold War situation. Institutional reforms should be also considered. The membership of the Security Council

should be reviewed taking into consideration its geographical composition and the question of the veto power. These considerations are indispensable as the concept of global security expands to include food supplies, natural resources, energy and the environment.

4. Concerning the peace-keeping operations of the United Nations, it is not easy to find an answer as to when, how, and why interventions should be made in the affairs of sovereign states. The only rationale would be intervention under international law, but international law itself is not universal. The question of providing an independent military force at the disposal of the United Nations to strengthen peace-keeping operations is controversial.
5. Nuclear weapons must be reduced with the ultimate aim of their total abolition. The same of course applies to other weapons of mass destruction. As for the international trade in weapons, major governments have been either assisting or promoting arms exports since the end of the Cold War. Reductions are essential, not only by purchasing countries, but should involve voluntary restrictions by the supplying countries. In addition, international cooperation continues to be needed in helping to eradicate international drug dealing, and governments must cooperate, including exchanging of information, to combat internationally organized terrorism.
6. Disputes and conflicts involving religions are rampant. The Moslem religion and Islamic fundamentalism should not be seen as identical, and it is wrong to link them with terrorism. In order to deepen mutual understanding between different religions and to prevent future religious conflicts, dialogues among religious and spiritual leaders are necessary to seek build a new paradigm for a universal ethical or value system. Such dialogues would also be used in the common task of countering the global erosion of morals.
7. Appropriate and stable monetary and fiscal policies are essential to stabilize international financial markets and exchange rates between national currencies. More positive disclosure of information concerning national and international economic and financial institutions is desirable by monetary authorities and international financial institutions. Such information alone will not be sufficient, given the colossal size of international capital flows. In particular, trading in financial derivatives is rapidly increasing, casting doubts on the stability of the financial markets. Such instruments, if used appropriately, can be useful to avert risk. While it would be an exaggeration to say that all of these trading are casino-like speculations, there is such an element in many dealings. Recent incidents demonstrate the point. It is essential for the respective authorities to consider enacting some regulations which would not undermine market forces, while individual parties engaged in trading endeavor to manage risks.
8. The G-7 Summit Conference has become too formalized. It should revert to the original objective of a forum for exchanges of views among top leaders. We recommend that the G7 be expanded to include Russia and China formally in view of their geopolitical, military and economic



INTERACTION COUNCIL

DOCUMENTS FROM THE 13TH SESSION

Tokyo, Japan

23-26 May 1995

1. Opening Statement by H. E. Takeo Fukuda
2. Opening Statement by H. E. Helmut Schmidt
3. Report on "Challenge to Balance Population Increase and Food Supply" by
H. E. Malcolm Fraser
4. Report on "The Future Role of Multilateral Institutions by H. E. Andries van Agt
5. Introductory Report on "Regulating the Globalized Financial Markets" by
H. E. Kurt Furgler
6. Summary of the Meeting at the Press Conference chaired by H. E. Pierre E. Trudeau

Mc

N

95 SEP 20 AM 10:06

World Bank/IFC/MIGA
OFFICE MEMORANDUM

RECEIVED
DEVELOPMENT ECONOMICS
ECONOMIST

DATE: September 19, 1995 10:04am

TO: Julia Ben Ezra

(JULIA BEN EZRA)

FROM: Claudia Fumo, OPRPG

(CLAUDIA FUMO)

EXT.: 31765

SUBJECT: Correspondence for Mr. Wolfensohn

Julia,

The NGO Unit had received two letters addressed to Mr. Wolfensohn - from the Rev. David Nelson and from a Mrs. Olive Tweed - which require a response but which I now have given to Valerie. We are simply not able to handle letters sent to Mr. Wolfensohn by single persons and these two letters are not from NGO representatives but from individuals expressing their opinions about the Bank.

Thanks very much,

Claudia

CC: Valerie Proute

(VALERIE PROUTE)

CC: John D. Clark

(JOHN D. CLARK)

*Jan, who should
these go to!
These are letters
criticizing the Bank's
structural adjustment
program. Syst
Hes to send it to
DEC*

HUMAN CAPITAL DEVELOPMENT
and
OPERATIONS POLICY
Vice Presidency

Assigned to: JC Clark	
Copied to:	
1. _____	
2. _____	
3. _____	
Action Required:	
1. URGENT	
2. Please prepare a reply for Mr. Choksi's signature.	
3. Please handle.	
4. For information.	
5. Other (see comments below).	
Re-assigned to:	
Due to HCOVP by: 9/20/95	
Reference No.: 0081	
File Under:	
Comments:	

RECEIVED
95 SEP 13 AM 10:46
CORRESPONDENCE MANAGEMENT FOR THE PRESIDENT'S OFFICE
CHORUS

95 SEP 14 PM 3:10
External Correspondence Profile
OPR/OPERATIONS POLICY

Reference #: EXC-02820

For Action: Armeane Choksi
VPU: HRO Room #: S-13-131 Telephone: 31811

Log Date: 09/12/95 06:37:41 PM
Status: Open
Response Date:

CORRESPONDENCE DESCRIPTION:

From: Rev. David Nelson
To: Mr. Wolfensohn
Dated: 09/07/95
Topic: opposition to "structural adjustment"

ACTION INSTRUCTIONS:

Due Date: 09/21/95

1. Please handle/respond on behalf of Mr. Wolfensohn and provide a copy to EXC.

SPECIAL INSTRUCTIONS:

None

INFORMATION COPIES:

Please return to:
Maree Aniba, EXC, E1227, 84138

508

111 Stafford St.
Stafford Springs, CT. 06076
Sept. 7, 1995

Mr. James D. Wolfensohn, President
The World Bank
1818 H St., NW
Washington, D.C. 20433

Dear Mr. Wolfensohn

I am writing to express my opposition to the way the World Bank supports "structural adjustment" in third world countries as a condition for loans. I believe that these programs hurt the developing country by forcing austerity upon it, thereby punishing its majority of poor people through cuts in social spending, wage suppression and privatization.

Instead of regressive practices, the World Bank should adopt the Grameen or grass roots type of loan - a small loan (\$50 or less) to a poor person or family who is part of a small group of borrowers who monitor payments of individuals in the group. Outside money starts the process and savings of borrowers provide additional capital. This grassroots approach can do more to upbuild a country's people than the large scale projects which benefit only those in power and their friends who get the work.

I hope that the Bank will reform speedily so that it becomes more of a help to poor countries rather than just a tool of the foreign policy of the industrialized nations.

Thank you.

Sincerely,



Rev. David Nelson

R	SEP 12 1995
	By 

Q

R

The World Bank

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

1818 H Street, N.W.
Washington, D.C. 20433
U.S.A.

(202) 477-1234
Cable Address: INTBAFRAD
Cable Address: INDEVAS

J W Chro

September 26, 1995

Mrs. Janet Rocher
#3 Cheshire Acre, Wirral
Merseyside L49 5LU
United Kingdom

Dear Mrs. Rocher:

On behalf of Mr. Wolfensohn, I am responding to your card of September 18, 1995, and your concern about the impact of structural adjustment programs on the poor. Mr. Wolfensohn is currently reviewing structural adjustment loans as part of his overall assessment of World Bank operations and will make modifications as required. From his observations so far, he has come to appreciate the value of well-designed adjustment programs for the poor. Hopefully, the Bank will improve quality in future operations, based on lessons learned from successful cases.

Thank you for your card and your concern.

Best wishes,

Lyn Squire

Lyn Squire, Director
Policy Research Department

The World Bank

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

1818 H Street, N.W.
Washington, D.C. 20433
U.S.A.

(202) 477-1234
Cable Address: INTBAFRAD
Cable Address: INDEVAS

June 1, 1995

Ms. Susan Ryan AO
Executive Director, ASFA
Level 19, Piccadilly Tower
133 Castlereagh Street
Sydney 2000, Australia

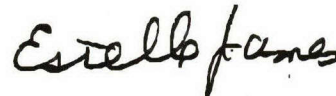
Dear Ms. Ryan:

Ellen Sullivan has passed on to me your invitation to give a presentation to the ASFA. I would be delighted to do that, and to learn from you how your new superannuation plan has been working. Since Australia's plan is one of the innovative models that we discuss in Averting the Old Age Crisis, I am especially anxious to hear about the problems you have encountered (every new plan encounters problems) and how you have been solving them.

I expect to be in Indonesia, and therefore not too far from Australia, this summer and hope it will be possible to coordinate my plans and yours. Although my schedule is not yet firm, the most likely dates that I could be in Sydney are July 13 or 14. Please let me know if this is convenient for you.

I look forward to hearing from you and meeting you.

Yours Sincerely,



Estelle James
Lead Economist, Policy Research Department,
World Bank

cc: Messrs./Mmes.: Malloch Brown, Ellen Sullivan, N. Barrett (EXC), L. MacDonald
Brown (EXTIM)

Room # N-5053
Phone (202) 473-7489
Fax (202) 522-1153

HUMAN RESOURCES DEVELOPMENT
and
OPERATIONS POLICY
Vice Presidency

0613

Assigned to:

M. Bumar

Copied to:

1.

L. Squire

2.

M. Baural

3.

M. Anison

Action Required:

1. URGENT

2. Please prepare a reply for Mr. Choksi's
signature

3. Please handle

4. For information

5. Other (see Comments below)

Re-assigned to:

Due to HROVP by:

Reference No.:

File Under:

Comments:

Squire Estelle is with you
Council you pls. handle. A

THE WORLD BANK GROUP

ROUTING SLIP		DATE: May 24, 1995	
NAME			ROOM. NO.
✓ Mr. Armeane Choksi			S13-131
cc: Mr. Malloch Brown			T8011
☐	URGENT	☐	PER YOUR REQUEST
☐	FOR COMMENT	☐	PER OUR CONVERSATION
☐	FOR ACTION	☐	NOTE AND FILE
☐	FOR APPROVAL/CLEARANCE	☐	FOR INFORMATION
☐	FOR SIGNATURE	☐	PREPARE REPLY
☐	NOTE AND CIRCULATE	☐	NOTE AND RETURN
RE: Letter from ASFA, Australia			
REMARKS: Regrets were sent to the original invitation to Mr. Wolfensohn. Please handle as appropriate. Thank you			
FROM Maree T. Aniba, Executive Assistant, EXC		ROOM NO. D12-074	EXTENSION 84138

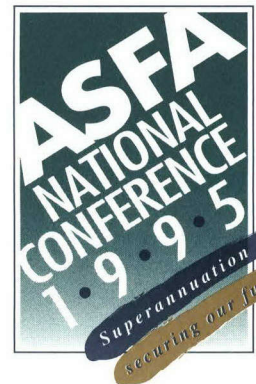
5/26 Kate -
 Lyn's slip is handling -
 Lane

RECEIVED
 DEVELOPMENT ECONOMICS
 & ENVIRONMENTAL
 ADMINISTRATION
 95 MAY 25 PM 4:47

18 May 1995

756
524
RECEIVED
25 MAY 24 PM 4: 03

HROVP



1 - 3 NOVEMBER 1995 - MELBOURNE

Mr James Wolfensohn
President
The World Bank
1818 H Street, N.W.
Washington, D.C. 20433
U.S.A.

Dear Mr Wolfensohn,

I am writing to you again to repeat my invitation to you of 7th April 1995 to be a plenary speaker at the annual conference of the Association of Superannuation Funds in Australia.

The conference will be held 1st - 3rd November 1995 in Melbourne and will be attended by in the vicinity of 1,500 delegates representing all sectors of the superannuation and investment industries.

We are particularly keen to have a speaker from the World Bank because of the great interest there is in Australia to the report, *"Averting the Old Age Crisis"*.

If you are unable to accept our invitation we would like to invite Estelle James, Economist, Policy & Human Resources Division at the World Bank. If you are able to accept our invitation of course I can assure you of optimal exposure to the industry and to the media in a highly favourable environment.

I look forward to hearing from you.

Yours sincerely,

Susan Ryan, AO
Executive Director



All correspondence to:
THE ASSOCIATION OF SUPERANNUATION FUNDS OF AUSTRALIA LIMITED ACN 002 786 290
LEVEL 19, PICCADILLY TOWER, 133 CASTLEREAGH STREET, SYDNEY 2000. (GPO BOX 1485, SYDNEY 2001)
TELEPHONE: (02) 264 9300, FACSIMILE: (02) 264 8824

The World Bank
Washington, D.C. 20433
U.S.A

079/
1. m. Boun
2. m. Boun

MES D. WOLFENSOHN
resident

95 DEC 20 AM 10:33

RECEIVED
DEVELOPMENT ECONOMICS
VP & CHIEF ECONOMIST

December 13, 1995

Mr. James Gustave Speth
Administrator
United Nations Development Programme
One United Nations Plaza
New York, NY 10017

Dear Gus:

I would like to thank you very much for joining me and the other UN Agency Heads at our day of meetings on November 28, 1995. I found our discussions to be very productive and enlightening. My colleagues were also very appreciative of the opportunity to participate in the meetings.

I believe that the day was extremely useful in furthering our goal of finding ways to build more effective partnerships between the UN system and the World Bank. I was remarkably impressed by the consensus on the issues and on the ways to address the common problems we face. I hope that the momentum for stronger and more effective collaboration started at our meeting will continue to grow at the operational level in all our organizations.

A number of suggestions for improving our collaboration came out of our discussions. On some of these, we are in the process of formulating recommendations for further action. Other suggestions will require a careful review by my colleagues before I can take any decision.

Among the suggestions in the first category, which are under active consideration, are those which relate to (a) the creation of a special rehabilitation fund for post-conflict situations, and (b) the preparation of technical assistance packages to assist the private sector in developing countries to gain access to global markets. The suggestions which require further review and analysis are those related to (a) the regular exchange of information between the Bank and the UN system, (b) making an increasing use by Bank borrowers of UN delivery capacity in the field, (c) the linkage between the Bank's Country Assistance Strategy (CAS) and the UN's Country Strategy Note (CSN). I have assigned each of these recommendations to a senior manager for follow-up and recommendations. I have also asked my colleagues to look more carefully at your

suggestions for the Bank to take the lead in the continuum from relief to reconstruction and to join the Inter-Agency Committee on Humanitarian Affairs. Mr. Timothy Thahane, Vice President for UN Affairs, will be following these initiatives carefully and will be available to discuss them with you. I will also be prepared to report to you further when we next convene.

There was a suggestion for the Bank to make regional loans to two or more countries in a particular geographical Region. Such loans could finance projects in the areas of environment or telecommunications. While many of our loans, particularly those in the environment and infrastructure, consider regional and cross-boundary dimensions, under its Articles of Agreement, the Bank cannot make regional loans. The same applies to IDA.

Thank you again for taking the time to spend a day with us here at the World Bank. I look forward to seeing you again soon.

With warm regards.

Sincerely yours,

(SIGNED) ~~James D. Wolfensohn~~

James D. Wolfensohn

cc: Messrs./Mmes. G. Kaji, S. Sandstrom, R. Lomax, M. Strong, J. Bassinette (EXC);
~~M. Bruno (DECVP)~~; A. Choksi (HCOVP); C. Koch-Weser (MNAV); I. Serageldin (ESDVP);
T. Thahane (SECV); J. Wood (SASVP); M. Malloch Brown (EXTDR); K. Dervis (EC2DR)

Similar letters sent to the following:

Ms. Carol Bellamy, Executive Director, UNICEF
Mr. Adnan Badran, Deputy Director-General, UNESCO
Mr. D.G. Aitken, Assistant Director-General, Who
Mr. Jean-Marc Deroy, Managing Director, UNIDO
Ms. Elizabeth Dowdeswell, Executive Director, UNEP
Mr. Howard Hjort, Deputy Director-General, FAO
Mr. Michel Hansenne, Director-General, ILO
Mr. A.N. Ngongi, Deputy Executive Director, WFP
Mrs. Sadako Ogata, High Commissioner, UNHCR
Dr. Nafis Sadik, Executive Director, UNFPA

OFFICE MEMORANDUM

DATE: October 24, 1995

95 OCT 25 AM 9:34

TO: Mr. James D. Wolfensohn, EXC

RECEIVED
DEVELOPMENT ECONOMICS
V.P. & CHIEF ECONOMIST

FROM: Mark Baird, Acting DECVP

EXTENSION: 31666

SUBJECT: **Relations with WTO**

Mr. Bruno had two meetings with Jesús Seade, Deputy Director-General of WTO, over the Annual Meetings period. The first, which was also attended by Mr. Boorman (IMF) and his staff, constituted the first meeting of the Working Group on Coherence in International Policy Making. Mr. Seade seemed surprised that the Bank and the Fund had done any thinking on this matter, and asked to see their preliminary internal documents. These have now been sent to him. He promised that the WTO would respond setting out their view of coherence relatively soon. The deputies to the working party have been asked to produce a draft report by March 1996, emphasizing the practical issues of coherence that could be addressed, and the Working Group will meet again in April 1996. The Fund and the Bank expressed the hope that the Working Group would complete its work by that time, but Mr. Seade's view was that it would probably take significantly longer.

The second meeting was on the Cooperation Agreement between the Bank and WTO. This was a constructive meeting which made significant progress on a draft agreement. However, major differences remain between the Bank and WTO over access to the Development Committee and to the Bank's Executive Board. Mr. Seade felt that the member governments of WTO would be unable to agree to any Cooperation Agreement which did not give WTO access to restricted sessions of the Development Committee and to at least some country-specific sessions of the Executive Board. Both issues caused the Bank side some difficulty--the Development Committee because the new format does not appear to be consistent with offering privileged status to WTO, and the Executive Board because the Board itself showed some reluctance to admit WTO to country-specific meetings. It was agreed that these matters would be reviewed after the WTO had discussed them with the Fund, but we understand from the Fund that, when they did so, the Fund was similarly unencouraging.

We have not yet heard from WTO how they wish to proceed following the meetings. However, it now seems clear that we cannot complete the Cooperation Agreement by November as originally planned. Mr. Bruno has asked IEC staff to keep in contact with WTO and to explore with them ways in which the various matters might be resolved. We will keep you informed.

c.c. Messrs./Mss. Frank, Kaji, Sandstrom, Lomax, Horiguchi (EXC),
Bruno (DECVP) o/r, Ahmed, Winters (IECIT)

Chiron

The World Bank
Washington, D.C. 20433
U.S.A.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

October 19, 1995

Ambassador Jesús Seade
Deputy Director-General
World Trade Organization
Centre William Rappard
Geneva
SWITZERLAND

Dear Jesús,

Cooperation and Coherence

It was a great pleasure to see you again last week and to be able to advance on the fronts of coherence and cooperation. I am sorry that time constraints precluded our spending longer on them.

I gather that after I left the meeting, the Coherence Working Group agreed that we should send you our preparatory work on coherence. I enclose this herewith. You will understand that it was a private briefing note to me not intended for circulation even within the Bank, and I trust that you will excuse its directness. However, since the meeting went well and we all wish to proceed expeditiously, I feel comfortable in transmitting it to you.

I found our meeting on the Cooperation Agreement most useful and we look forward to receiving your revised draft agreement as soon as convenient. On the outstanding issues of the Development Committee and your attendance at country-specific Board meetings, we agreed to consider the situation once you had spoken further with the Fund.

As a general principle I suggest that we ask our deputies to look after the exchange of documents and the initial stages of the discussion. Perhaps you would ask your deputy to call Alan Winters to let us know how matters stand with the Fund. They can then review the positions on both coherence and cooperation and explore some options for moving forward.

It was good to see you in Washington and I look forward to our working further together.

Best wishes,

Yours sincerely,



Michael Bruno

Mr. Jesús Seade

2

October 19, 1995

b.c.c. M. Ahmed, L.A. Winters

LAW:akw

Bank/Fund/WTO Working Group on Coherence in International Policy Making

Background Note

L. Alan Winters

This note presents some initial thoughts about forthcoming discussions on coherence in international policy making with the WTO and the Fund. It suggests a working definition and operationalization of coherence, a list of some issues that might be taken up under that heading and suggestions about how they might be handled procedurally. It concludes with two proposals about the organization of the Working Party.

I have discussed the situation with Ms. Kirmani of the Fund, but have heard nothing from WTO except that they would like to discuss coherence during the Annual Meetings period. I believe that, as per your letter to Mr. Seade of October 4, we should just seek to delineate the activities of the Working Group and discuss procedure.

(A) Definition

The WTO agreement, Article III.5 states:

“With a view to achieving greater coherence in global economic policy making, the WTO shall cooperate, as appropriate, with the International Monetary Fund and with the International Bank for Reconstruction and Development and its affiliated agencies.”

Despite a large amount of talk about and strong commitment to coherence, the WTO has not yet offered any definition or suggestions about what it might entail. It is obviously for them to offer their own definition in their own time, but it seems useful for us to have something to offer for the meeting.

I can think of no better definition than that which the Fund is proposing in its preliminary (and also confidential) paper:

“to define the achievement of greater coherence in global policymaking as efforts by the three institutions, individually and collectively, to work towards harmonious implementation of their common and complementary objectives.”

In the terms of this definition, the institutions are already pursuing coherence, but one might accept that there is room to do more and that new issues will arise which fall under its rubrics. Three important aspects of the definition are that

- it avoids specifying a new set of objectives under the heading of coherence;
- it avoids introducing new standards against which “coherent” policies should be appraised; and
- it focuses on areas where the institutions have natural interfaces.

In operationalizing this definition we should also seek to keep coherence at the level of broad objectives and systemic issues, leaving matters surrounding the consistency of specific policy and advice under the rubric of the cooperation agreement.

The Bank and the WTO share one formal objective. The WTO is charged with “raising standards of living, ensuring full employment, and a large and steadily growing volume of real income and effective demand, and expanding production of and trade in goods and services,” while the Bank is enjoined to “promote the long range balanced growth of international trade... by assisting in raising productivity, the standard of living and conditions of labor in their territories.”

In addition, the WTO has two formal objectives which match very closely with the way in which the Bank interprets its role:

To allow “for the optimal use of the world’s resources in accordance with sustainable development, seeking both to protect and preserve the environment,

“to ensure that developing countries... secure a share in the growth in international trade commensurate with the needs of their economic development.”

In addition to these common objectives, the WTO’s and Bank’s roles are highly complementary in a number of dimensions:

Both are concerned with trade liberalization, the Bank with unilateral liberalization that need not be bound internationally, and the WTO with multilateral liberalization which must be bound.

The Bank sees the international trading system as an essential tool for development policy, while WTO sees it, more or less, as its *raison d’être*.

The Bank assesses a developing country’s trade policies in the course of its standard economic work and makes recommendations upon it, while the WTO undertakes an occasional formal review of international trade policy under its Trade Policy Review Mechanism.

Both institutions undertake a certain amount of technical assistance which generally is, and certainly should be, non-duplicative.

These common and complementary objectives leave plenty of scope for coherence discussions.

(B) Possible Issues for Bank-WTO Coherence Discussions

The following list comprises mainly the issues on which the Bank might seek WTO's assistance in attaining coherence. The section concludes, however, with one potentially sensitive issue of which we must be careful.

1. Export Prospects for Developing Countries

Many countries' development strategies depend on export growth. Although most of the responsibility for this falls on the developing country itself, the external environment sometimes looks rather hostile. Among the industrial country policies that give this impression are the long phase-out of the MFA, frequent anti-dumping actions, and high agricultural protection. These barriers are all sanctioned by WTO and the Bank would be helped in its mission if WTO could reduce the scope for them.

2. Developing Country Import Regimes

Developing country import regimes frequently entail undesirable policies that are WTO-consistent--e.g., QRs for safeguards and balance of payments purposes, and anti-dumping. The cover given to these policies by the GATT greatly complicates Bank efforts at rationalizing them. On the other hand, however, Bank activities aid WTO's mission in this area. Bank-led liberalizations improve access for exporters and offer significant strengthening of the trading system. The prohibition of cross-conditionality precludes the Bank from insisting that liberalizations be bound, but the Bank strongly promotes WTO membership.

In the context of membership, the negotiating aspect of the accession process can lead governments to postpone liberalizations in order, they claim, to keep some negotiating chips for that process. Similarly, some developing countries have held back unilateral liberalizations in anticipation of the Round. Clearer credit for liberal policies--for example, recognizing that binding a previous unilateral reduction of x% should be equivalent to binding a reduction of x% that is conditional on similar action by trading partners--would be useful.

3. Developing Country Export Regimes

Several countries--especially those in transition--have export restrictions. The GATT is formally less concerned about these than about import restrictions and is, de

facto, rather relaxed about them. Again this hinders Bank efforts at rationalization in a vital area of policy.

4. **Regionalism**

Neither the WTO nor the Bank is a great fan of regional trading blocs but neither has completely castigated them. A coherent position would be very desirable if it could be devised. This could extend beyond trade preferences to matters of deeper integration, such as the harmonization of standards, tax coordination and factor movements.

5. **Privatization**

The Bank strongly encourages the commercialization or privatization of state enterprises. Clearer assurance about how debt forgiveness will be treated under countervailing duties law and how firms can attain market status under anti-dumping law would be useful.

6. **New Trade Disciplines**

The Bank has a major interest and considerable experience in foreign direct investment and may wish to have an input into any future negotiations in WTO on an investment code. Similarly, the Bank has periodically advised countries on competition policy and would have an interest in any restrictions that WTO members sought to introduce in that area. Labor and environmental standards are issues which might threaten the liberal trading environment. The Bank would hope to be able to contribute directly to the debate in WTO in favor of liberalism and its developing country clients.

It is for WTO to define its own objectives under coherence, but I can think of one sensitive issue that might arise.

7. **Cross-conditionality**

There may be a temptation to view Bank and Fund conditionality as a means of aiding the implementation of the Uruguay Round. This is precluded by the prohibition of cross-conditionality. What is not precluded, but which some developing countries had apparently hoped to prevent, is that the Bank and the Fund go beyond the Uruguay Round, by, for example, suggesting an accelerated timetable on services liberalization. We must ensure that coherence and consistency do not prevent our doing this.

(C) Coherence Procedures

The Bank and WTO might pursue coherence at three levels. Day-to-day cooperation and the exploration of common interests at the conceptual level would rely on informal collaboration between working level staff of the two organizations. More strategic issues would be handled at periodic senior staff and Heads of Institution

meetings. It has already been agreed that there will be regular senior staff meetings (annually or perhaps more frequently at first) and the Heads of Institutions apparently intend to lunch together every quarter. The Board, and WTO equivalent, might be informed of the nature of these discussions and may offer advice on the issues concerned where appropriate, but I would not envisage an active role for them.

At the highest, ministerial, level issues of coherence may figure in certain meetings of the Development Committee, at which the Director-General of WTO might be invited to speak, and at the WTO's Ministerial Conference, which might be addressed by the Bank's President or his representative. We would expect to bring matters to this level only after full discussion at the other levels.

(D) Next Steps

The Working Party needs to devise a timetable and an operating procedure for itself. Given the seriousness of the issues it should not be rushed, but, on the other hand, it is desirable that these issues be resolved in the relatively near future. I suggest the following two fixed points:

(a) An agreed agenda should be produced by April 1996. I suggest that the principals ask their deputies to present a draft discussion agenda by March 1996 for final discussion and formal adoption in April around the time of the Spring Development Committee. The deputies might exchange preliminary drafts by, say, December.

(b) The Working Group should produce a report on coherence and how it might be improved no later than October 1996. We should try to avoid a formal agreement couched in legal form because coherence seems, at least at present, to be so vague and changing a concept that no side is likely to wish to bind itself significantly in such a form. Thus substance is more likely to be achieved by a less formal approach. We may not need a full year to achieve agreement, but until the agenda is fixed, that cannot be foretold. Several of the issues that might be discussed would require broad discussion within the Bank for which we should allow ample time.

063

HUMAN CAPITAL DEVELOPMENT
and
OPERATIONS POLICY
Vice Presidency

95 SEP 20 AM 10:51

RECEIVED
DEVELOPMENT ECONOMICS
UNIT ECONOMIST

Assigned to: <i>DEC</i>	
Copied to: <i>should go to (structure unit) DEC for a reply.</i>	
1. _____	
2. _____	
3. _____	
Action Required:	
1. URGENT	
2. Please prepare a reply for Mr. Choksi's signature.	
3. Please handle.	✓
4. For information.	
5. Other (see comments below).	
Re-assigned to:	
Due to HCOVP by: <i>09/26/95</i>	
Reference No.: <i>0088</i>	
File Under:	
Comments:	

Fr. Dorothy Scott Smith

CORRESPONDENCE MANAGEMENT FOR THE PRESIDENT'S OFFICE
CHORUS
External Correspondence Profile

Reference #: EXC-03067

For Action: Armeane Choksi VPU: HRO Room #: S-13-131 Telephone: 31811	Log Date: 09/18/95 06:03:51 PM Status: Open Response Date:
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CORRESPONDENCE DESCRIPTION:

From: Dorothy Scott Smith To: Mr. Wolfensohn Dated: 09/14/95 Topic: Rejection of the LAP - Structural Adjustment

ACTION INSTRUCTIONS:

Due Date: 09/27/95

1. Please handle/respond on behalf of Mr. Wolfensohn and provide a copy to EXC.

SPECIAL INSTRUCTIONS:

none

INFORMATION COPIES:

Please return to: Maree Aniba, EXC, E1227, 84138
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EXC-03067
09/27/95 10:26 AM
JACQU

0087

EXC 5067



LOVE

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WENE DL 2001

President
The World Bank
1818 H. St., N.W.
Washington, D.C.
20433

Dorothy Scott Smith
1425 A1A Highway Apt. 23
Satellite Beach, FL
32937-5408



9-14-95

Dear World Bank President:
Please halt Structural
Adjustment Programs that
deny credit to Third World
farmers who grow basic food
crops.

Please reject the LQIP
programs that force massive
spending cuts for health care
programs that benefit the
poor in developing countries.

Please stop short-sighted
LQIP programs that balance
budgets by laying off teachers
& closing schools in Central
America & elsewhere.

Please say NO to LQIP programs
that fill the pockets of the rich &
keep misery upon misery on the poor.

Please say YES to economic
policies that support efforts in developing
countries to provide food, health care &
education for all the people.

Please, love & joy to all.

Dorothy Scott Smith

0554

JAMES D. WOLFENSOHN

**1818 H STREET, N.W.
WASHINGTON, D.C. 20433**

Phone: (202) 458-5120
Fax: (202) 522-3433

May 3, 1995

Mr. Stanley S. Shuman
711 Fifth Avenue
New York, N.Y. 10022

Dear Stan:

Thank you for your letter of April 17, 1995 and for the information about the Center for International Development Research. The World Bank is interested in establishing and maintaining contact with research and training centers throughout the world. In this respect, I was pleased to see that both the Economic Development Institute and the Policy Research Department are interacting with CIDR. I would expect such interaction to continue.

Best regards,

ATs in J.W. file.

The World Bank
Washington, D.C. 20433
U.S.A.

MICHAEL BRUNO
Vice President Development Economics
and Chief Economist

May 3, 1995

Dear Jim:

The following is in response to your enquiry about DEC's involvement with the Center for International Development Research (CIDR) at Duke University.

Both the Economic Development Institute (EDI) and the Policy Research Department (PRD) have had involvement with the Center for International Development Research at Duke University.

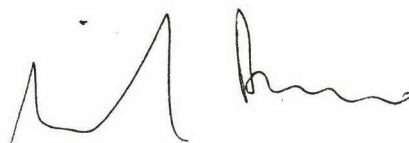
Economic Development Institute

As part of its program to assist countries with policy formulation, EDI has contracted with a number of institutions to develop teaching cases, including Duke's CIDR. The CIDR has recently completed a case study on *Social Safety Nets in the Ukraine*. In addition, they have started work on a case study on *Public Investment Programs* in Turkey and will soon be embarking on a generic case on *Trade Policy and Adjustment*.

Policy Research Department

CIDR runs a one-year *Program in International Development Policy* for policymakers from developing countries and a two-year *Masters in Public Policy* program. World Bank staff members are sometimes invited to make presentations on the Bank's work to CIDR students. Most recently Dominique van de Walle from the Public Economics Division gave a talk on her recently edited volume Public Spending and the Poor: Theory and Evidence. The book is being used in one of the Center's graduate courses. The mid-career students also take an annual trip to Washington during which they visit the Bank. Last year, Sanjay Pradhan of PRDPE spoke to the group about public expenditure issues and structural adjustment.

Sincerely,



Best regards

M

T

0419
006 Decv2

HUMAN CAPITAL DEVELOPMENT
and

OPERATIONS POLICY
Vice Presidency

3:12

Messrs. Ahmed/Lateef 9/25/95

Masood/Sarwar:

My feeling is that this type of letter should be passed to EXT for response, or did it go from them to AC?

Please, could you either respond by due date with a copy to Michael; or advise of other disposition.

Thanks

Kate

Att.

*This is urgent
an ext. response
type. Please handle
accordingly*
[Signature]

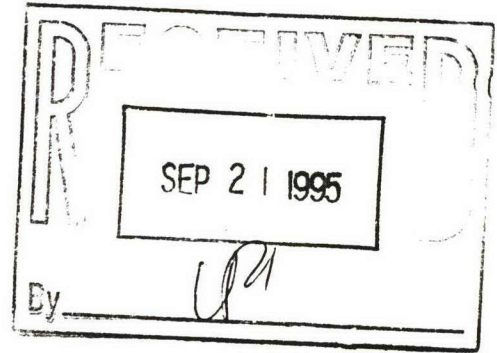
— Sent to EXT. 9/29 Maria

Assigned to: RECEIVED DEVELOPMENT ECONOMICS OFFICE	
Copied to: 1. _____ 2. _____ 3. _____	
Action Required:	
1. URGENT	
2. Please prepare a reply for Mr. Choksi's signature.	
3. Please handle.	
4. For information.	
5. Other (see comments below).	
Re-assigned to: DEC	
Due to HCOVP by: 1	
Reference No.: 0095	
File Under:	
Comments:	

September 16, 1995

1162 Mallard Creek Road
Louisville, KY 40207

James Wolfensohn, President
c/o the World Bank
1818 "H" St. NW
Washington, DC 20433



Dear Mr. Wolfensohn:

I have recently become more informed about some of the policies of the World Bank and IMF. Even though the intent 50 years ago was meant to better the conditions of humanity, they have in fact, burdened the poor and increased disadvantages. The international debt has become a major obstacle to human development and protection of the environment. Structural Adjustment Programs too often place the burden of debt on the poorest by insisting that national budgets be used first to pay interest on the debt. This leaves only crumbs for schools, clinics, housing, water systems, and credit for small farmers and businesses. The result around the world has been increased poverty and misery for hundreds of millions of people. This has got to stop!

I encourage you at the Annual meetings in early October to candidly assess the sin in the global economy. Take an honest look at the suffering imposed by world monetary and economic policy on those who have the least. Pursue God's vision of a new heaven and a new earth grounded in compassion, equity and justice. Forgive debts!

I strongly urge you and other leaders of the World Bank and IMF to reorient the priorities of the international financial institutions to ensure the development of sustainable communities, respect for the integrity of creation, and the provision of basic human needs for all. Further, it is critical to lift the debt carried by the human communities and environment of impoverished nations. World Bank and IMF reserves need to cancel the multilateral debt of severely indebted low and lower-middle income countries. Finally, I urge the World Bank and IMF to radically alter or end structural adjustment programs that have exacerbated the suffering of the poor.

Thank you for your willingness to be of courage and reassess the ways of the World Bank and IMF at this time.

Sincerely,

Rebecca J. Tollefson

Rebecca J. Tollefson

cc: Senator Mitch McConnell, Religious Working Group of the World Bank and the IMF

**CORRESPONDENCE MANAGEMENT FOR THE PRESIDENT'S OFFICE
CHORUS**

External Correspondence Profile

RECEIVED
SEP 22 AM 11:37
HROVP

Reference #: EXC-03151

For Action: Armeane Choksi

VPU: HRO Room #: S-13-131 Telephone: 31811

Log Date: 09/22/95 08:31:06 AM

Status: Open

Response Date:

CORRESPONDENCE DESCRIPTION:

From: Rebecca J. Tollefson

To: Mr. Wolfensohn

Dated: 09/16/95

Topic: Structural Adjustment Programs - Inflicting the poor with burdens

ACTION INSTRUCTIONS:

Due Date: 10/03/95

1. Please handle/respond on behalf of Mr. Wolfensohn and provide a copy to EXC.

SPECIAL INSTRUCTIONS:

none

INFORMATION COPIES:

Please return to:

Maree Aniba, EXC, E1227, 84138

0095

002

HUMAN CAPITAL DEVELOPMENT
and
OPERATIONS POLICY
Vice Presidency

DEC

95 SEP 20 AM 10:51

RECEIVED
DEVELOPMENT ECONOMICS
UNIT
ECONOMIST

Assigned to: <u>J. Clark</u>	
Copied to:	
1. _____	
2. _____	
3. _____	
Action Required:	
1. URGENT	
2. Please prepare a reply for Mr. Choksi's signature.	
3. Please handle.	
4. For information.	
5. Other (see comments below).	
Re-assigned to:	
Due to HCOVP by: <u>9/20/95</u>	
Reference No.: <u>0084</u>	
File Under:	
Comments:	

fr: Olive Tweed

RECEIVED
CORRESPONDENCE MANAGEMENT FOR THE PRESIDENT'S OFFICE
CHORUS

95 SEP 14 24 3:10
External Correspondence Profile
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SEP 13 AM 10:47
HROVP

Reference #: EXC-02821

For Action: Armeane Choksi VPU: HRO Room #: S-13-131 Telephone: 31811	Log Date: 09/12/95 06:39:41 PM Status: Open Response Date:
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CORRESPONDENCE DESCRIPTION:

From: Mrs. Olive Lweed To: Mr. Wolfensohn Dated: 09/07/95 Topic: Advice handed out by the World Bank & IMF is flawed

ACTION INSTRUCTIONS:

Due Date: 09/21/95

1. Please handle/respond on behalf of Mr. Wolfensohn and provide a copy to EXC.

SPECIAL INSTRUCTIONS:

None

INFORMATION COPIES:

Please return to: Maree Aniba, EXC, E1227, 84138
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0074

Exc 2821

21, Ambleside Court,
Coughdon, Gheslin
 ENGLAND
 CW12 4HZ
 7th Sept. 1995

Dear President,

In the wake of celebrations for peace marking the end of the world war struggles of 50 years ago, it is now time to remember the organisations which were set up at that time to help people cope with the devastation caused by these conflicts. Christian Aid was one of these & World Bank & I.M.F. others

I can speak from first hand knowledge of Christian Aid policies which have attempted to adapt to the needs of the recipient nations. With the demise of imperialism we now properly regard these as partners - in other words equals in God's eyes. Who better than those who have to struggle with poverty - sometimes caused by extremes of climate, sometimes by war, with ensuing disease - know what is workable at grass roots level? This partnership where they take the initiative in terms of ideas, actually works far better than anything we westerners could devise with our tunnel vision, market values, 'assumed' superiority & isolationist types of relationship. ORAP (Organisation for Rural Associations for Progress) is one such group which Christian Aid supports in Zimbabwe. Two ideals are used by ORAP - 'Zenzele' means to do it yourself, and 'Amarima' describes the system of families supporting each other, based on traditional Zimbabwean customs. About 5 families are organised into units, which in turn form larger & larger groups, eventually making up 18 associations. ORAP now has about a million members organised in this way.

Each family unit meets weekly to share ideas, understand

the reasons for their problems & seek to solve these themselves. This community organisation is as important a part of ORAP's work as providing practical help & loans for projects, and is in marked contrast to the purely economic approach of World Bank policies.

In the 1995 global village to which we all belong, our neighbours in what we glibly call the Third World are suffering untold misery & high mortality of all age groups. This is due in no small measure to the present policies of the World Bank & I.M.F. The structural adjustment programmes are a crippling burden which no-one should be required to bear. Surely it is better to cut our losses & accept that much of the debt on loans, which to my understanding were not properly ^{research} & monitored anyway as recently as the 1980's, cannot be repaid.

I write as a U.K. taxpayer who gives £10 a year to the World Bank & I.M.F. & at present have no say in how it is spent. Human rights in our own highly privileged western countries has moved on a pace in the latter half of this century. Surely the vast majority in our world are entitled to a more human policy. I believe South Africa won through from the gross injustices of apartheid, largely because God will not be mocked forever!

So how about celebrating the 50th anniversary of the World Bank & I.M.F. by scrapping the SAP's programme & returning to the original purposes for which they were set up i.e. enabling those who were suffering & broken to achieve self-respect & hope in some kind of future?

P.S. I enclose a copy of a recent letter to my M.P. on the same subject.

Yours faithfully

Olive Lweed (Mrs)

10 Mrs. A. Winkerton, M.P. for Congleton,
House of Commons,
Westminster, London SW1A 0AA

(Copy)

21, Hudderside Court,
Congleton, Cheshire
CW12 4HZ
1st Sept. 1992

Dear Ann,

Christian Aid is running the campaign which asks 'Who Runs the World' which challenges the policies of the World Bank & I.M.F. Our objective is to find ways of discovering people-friendly alternatives to Structural Adjustment Programmes which are at present crippling the poor, particularly in Jamaica. (see flyer)

Britain has an opportunity to make good use of past expertise in areas of international policy in development, peacekeeping & emergency relief.

A long-term strategy is needed with a clear focus on poverty reduction as well as on sustainable growth. Long-term strategy will also need to address failures in the market. The advice handed out by the World Bank & I.M.F. is flawed. Several countries are being asked to expand the sales of the same product with a subsequent world-wide glut, resulting in depression of prices, farmers have to work much harder to produce their 'cash crops' in order to sell more - only to earn less! This kind of injustice is disastrously short sighted & utterly wrong!

Justice has been part of Britain's heritage over the years, I believe that the world still looks to us for a lead in this area. Our policy towards the struggling Third World countries should bear this in mind & not be driven by short-term economic interests.

I understand that the Chancellor of the exchequer Kenneth Clarke is due to attend the annual meeting of the World Bank & I.M.F. in October. I would appreciate it if you would ask him to address the criticism on that occasion. Also to consider carefully our own financial commitment in order that our overseas aid budget is protected from further real reductions.

Thank you for your past help in expressing my point of view to the press concerned. I enclose a 'flyer' which asks for your own commitment to the above issues. I hope you will be able to align yourself with us in Christian Aid & add the weight of your shoulder to the wheel?

Yours sincerely

Olivia Lloyd

The World Bank
Washington, D.C. 20433
U.S.A.

JAMES D. WOLFENSOHN
President

August 31, 1995

Mr. Arthur R. Taylor
President
Muhlenberg College
Allentown, PA 18104-5586

Dear Arthur:

Thank you for your letter and good wishes.

I looked at the note prepared by Professor Kleinman. His proposal to promote the flow of long-term capital to developing countries and enhance the stability of such flows is interesting, but may not be easily implementable and raises a number of issues, such as the moral hazard of official actions, that need to be carefully considered.

I have asked Mr. Masood Ahmed, Director, International Economics Department, to review the note and respond directly to Professor Kleinman.

It is nice to hear from you again.

Wam good with

Sincerely yours,

W

James D. Wolfensohn

Hope all goes well with you

bcc.: Messrs./Mme. Bruno (DECVP); Ahmed, Bhattacharya (IECDR);
Khambata (CCMDR); Perlin (FSDDR)

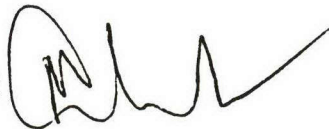
Ch. Wolfensohn

OFFICE MEMORANDUM

DATE: August 31, 1995

TO: Maree Aniba, EXC

FROM: Masood Ahmed, Director, IEC



EXTENSION: 33800

SUBJECT: **Response to Arthur R. Taylor**

Attached is a draft response from Mr. Wolfensohn to the letter from Arthur R. Taylor.

We in DEC have had no contact with Professor Kleinman, but Gary Perlin and Farida Khambata who have had prior discussions with him, have reservations about his work and its usefulness.

As to the specific proposal that he puts forward in the note sent to Mr. Wolfensohn on promoting greater stability in capital flows to developing countries, we have the following concerns:

- First, it is not clear that the illiquidity is the major cause for fluctuations in emerging markets, rather than changes in perception of fundamentals.
- Second, the potential magnitude of swings is so large that extending the limited resources available to international development institutions to provide margin credit to dealers is not likely to be effective, and could expose these institutions to large losses.
- Third, and most importantly, extending such credit would raise serious moral hazard problems that could undermine the efficient functioning of global capital markets.

We do not propose that Mr. Wolfensohn cite these concerns directly in his letter. Instead, I propose to send a follow-up letter to Professor Kleinman raising these issues.

Attachment

cc: Messrs./Mme. Bruno (DECVP), Perlin (FSDDR), Khambata (CCMDR),
Bhattacharya (IECDR)

0289

Correspondence Management for the President's Office
CHORUS

External Correspondence Profile

Reference #: EXC-01801

For Action: Michael Bruno
VPU: Room #: Telephone:

Log Date: 08/24/95
Status: Open
Response Date:

Correspondence Description:

From: Arthur R. Taylor, Muhlenberg College
To: Mr. Wolfensohn
Dated: 07/31/95
Topic: sending article from Dr. David Kleinman

Action Instructions

Due Date: 08/31/95

3. Please prepare a response for Mr. Wolfensohn's signature.

Then please send the copy of the letter for Mr. Wolfensohn's signature back to Maree in E1227 together with the copy of the Log Sheet and incoming letter. In addition, please enclose two copies of the response letter which show the bccs, drafter's ID and EXC log number. These copies will be stamped " (signed) JAMES D. WOLFENSOHN ". Once the letter is signed, Ms. Kathy Ray will call your office. You can pick up the signed letter together with one "stamped" copy showing the bccs from D12069. VP Units are responsible for distribution of the original signed letter and the copies.

Special Instructions

personal mail. JDW wrote a note to Michael Bruno (or anyone!) and DEC "Does anyone know about this man and his work i.e., Kleinman." dated 08/11/95. - forwarded to Farida Khambata, CCMDR and Gary Perlin, FSD. Returned to M. Bruno to respond - 8/24/95.

Mr. Wolfensohn has seen the note from F. Khambata.

Information Copies:

Please return to:
Maree Aniba, EXC, E1227, 84138

95 AUG 24 PM 3:13

RECEIVED
DEVELOPMENT ECONOMICS
& POLICY UNIT

THE WORLD BANK GROUP

ROUTING SLIP		DATE: August 16, 1995	
NAME		ROOM. NO.	
Mr. Masood Ahmed		N4 043	
☐	URGENT	☐	PER YOUR REQUEST
☐	FOR COMMENT	☐	PER OUR CONVERSATION
☒	FOR ACTION	☐	NOTE AND FILE
☐	FOR APPROVAL/CLEARANCE	☐	FOR INFORMATION
☐	FOR SIGNATURE	☐	PREPARE REPLY
☐	NOTE AND CIRCULATE	☐	NOTE AND RETURN
☐		☐	
RE: Correspondence from A Taylor to J Wolfensohn			
REMARKS: Masood: Please see JW's note. Can we help or should I pass on to IFC? The deadline to Maree Anibe is August 21. Thanks Kate cc. V Thomas, Acting VP DEC May I have a copy of the response for DEC files? <i>I would pass on to Gary Perlman & Faride Khankata. They will be placed to comment on this. Masood -</i>			
FROM Kate Oram		ROOM NO. N6 045	EXTENSION 31107

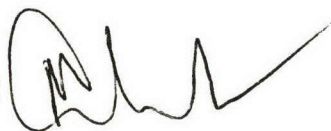
OFFICE MEMORANDUM

H. Wolfensohn

DATE: August 31, 1995

TO: Maree Aniba, EXC

FROM: Masood Ahmed, Director, IEC



EXTENSION: 33800

SUBJECT: **Response to Arthur R. Taylor**

Attached is a draft response from Mr. Wolfensohn to the letter from Arthur R. Taylor.

We in DEC have had no contact with Professor Kleinman, but Gary Perlin and Farida Khambata who have had prior discussions with him, have reservations about his work and its usefulness.

As to the specific proposal that he puts forward in the note sent to Mr. Wolfensohn on promoting greater stability in capital flows to developing countries, we have the following concerns:

- First, it is not clear that the illiquidity is the major cause for fluctuations in emerging markets, rather than changes in perception of fundamentals.
- Second, the potential magnitude of swings is so large that extending the limited resources available to international development institutions to provide margin credit to dealers is not likely to be effective, and could expose these institutions to large losses.
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We do not propose that Mr. Wolfensohn cite these concerns directly in his letter. Instead, I propose to send a follow-up letter to Professor Kleinman raising these issues.

Attachment

cc: Messrs./Mme. **Bruno** (DECVP), Perlin (FSDDR), Khambata (CCMDR),
Bhattacharya (IECDR)

The World Bank

Washington, D.C. 20433
U.S.A.

JAMES D. WOLFENSOHN
President

August 31, 1995

Mr. Arthur R. Taylor
President
Muhlenberg College
Allentown, PA 18104-5586

Dear Arthur:

Thank you for your letter and good wishes.

I looked at the note prepared by Professor Kleinman. His proposal to promote the flow of long-term capital to developing countries and enhance the stability of such flows is interesting, but may not be easily implementable and raises a number of issues, such as the moral hazard of official actions, that need to be carefully considered.

I have asked Mr. Masood Ahmed, Director, International Economics Department, to review the note and respond directly to Professor Kleinman.

It is nice to hear from you again.

Warm good wishes

Sincerely yours,

JDW

James D. Wolfensohn

Hope all goes well with you

bcc.: Messrs./Mme. **Bruno** (DECVP); Ahmed, Bhattacharya (IECDR);
Khambata (CCMDR); Perlin (FSDDR)

Noted in DECUP ^{108 #} 0289

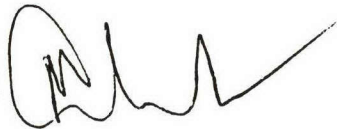
THE WORLD BANK/IFC/M.I.G.A.

OFFICE MEMORANDUM

DATE: August 31, 1995

TO: Maree Aniba, EXC

FROM: Masood Ahmed, Director, IEC



EXTENSION: 33800

SUBJECT: **Response to Arthur R. Taylor**

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- Second, the potential magnitude of swings is so large that extending the limited resources available to international development institutions to provide margin credit to dealers is not likely to be effective, and could expose these institutions to large losses.
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cc: Messrs./Mme. Bruno (DECVP), Perlin (FSDDR), Khambata (CCMDR),
Bhattacharya (IECDR)

August 31, 1995

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President
Muhlenberg College
Allentown, PA 18104-5586

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James D. Wolfensohn

August 31, 1995

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President
Muhlenberg College
Allentown, PA 18104-5586

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Sincerely yours,

James D. Wolfensohn

bcc: Messrs./Mme. Bruno (DECVP); Ahmed, Bhattacharya (IECDR); Khambata (CCMDR); Perlin (FSDDR)

A. Bhattacharya
EXC-01801

THE WORLD BANK GROUP

ROUTING SLIP		DATE: August 24, 1995	
NAME			ROOM. NO.
Mr. Masood Ahmed			N4 045
☐	URGENT	☐	PER YOUR REQUEST
☐	FOR COMMENT	☐	PER OUR CONVERSATION
☒	FOR ACTION	☐	NOTE AND FILE
☐	FOR APPROVAL/CLEARANCE	☐	FOR INFORMATION
☐	FOR SIGNATURE	☐	PREPARE REPLY
☐	NOTE AND CIRCULATE	☐	NOTE AND RETURN
☐		☐	
RE: Correspondence Re D Kleinman(A Taylor to J Wolfensohn)			
REMARKS: Masood, As you see, this is back to us again! I guess someone has to prepare a response to Mr. Taylor for JW's signature. As both Perlin and Khambata know Kleinman, and we don't, I would have thought they could have dealt with it. If they don't think highly of him why are they suggesting that we (who don't know him) invite him to give a seminar. Perhaps you might discuss with Guy. In any event, I leave it in your expert hands but please note our new deadline to JW is August 31. Many thanks. Kate Att./-			
FROM Kate Oram		ROOM NO. N6 043	EXTENSION 31107

Correspondence Management for the President's Office
CHORUS
External Correspondence Profile

Reference #: EXC-01801

For Action: Michael Bruno VPU: Room #: Telephone:	Log Date: 08/24/95 Status: Open Response Date:
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Correspondence Description:

From: Arthur R. Taylor, Muhlenberg College To: Mr. Wolfensohn Dated: 07/31/95 Topic: sending article from Dr. David Kleinman

Action Instructions

Due Date: 08/31/95

3. Please prepare a response for Mr. Wolfensohn's signature.

Then please send the copy of the letter for Mr. Wolfensohn's signature back to Maree in E1227 together with the copy of the Log Sheet and incoming letter. In addition, please enclose two copies of the response letter which show the bccs, drafter's ID and EXC log number. These copies will be stamped " (signed) JAMES D. WOLFENSOHN ". Once the letter is signed, Ms. Kathy Ray will call your office. You can pick up the signed letter together with one "stamped" copy showing the bccs from D12069. VP Units are responsible for distribution of the original signed letter and the copies.

Special Instructions

personal mail. JDW wrote a note to Michael Bruno (or anyone!) and DEC "Does anyone know about this man and his work i.e., Kleinman." dated 08/11/95. - forwarded to Farida Khambata, CCMDR and Gary Perlin, FSD. Returned to M. Bruno to respond - 8/24/95.

Mr. Wolfensohn has seen the note from F. Khambata.

Information Copies:

Please return to: Maree Aniba, EXC, E1227, 84138

95 AUG 24 PM 3:47
100-100000000
100-100000000
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August 21, 1995

Ms. Maree Aniba

Re: Mr. David Kleinman

Michael Bruno sent the attached correspondence from Mr. Arthur Taylor to Mr. Wolfensohn to Gary Perlin and me. We have mixed feelings about Professor Kleinman who is known to us and whose work we have seen in the past. Prof. Kleinman would like to discuss with international institutions possible mechanisms that could be put in place to prevent or reduce the impact of another Mexico-type crisis. If what Prof. Kleinman would like (and this is not clear from his correspondence) is to have a forum to espouse his views, Michael Bruno and/or Guy Pfefferman of the Bank's and IFC's Economics Departments, respectively, might be requested to include Professor Kleinman when the next appropriate forum is organized.

Farida Khambata

Farida Khambata

cc: Mr. Perlin

MUHLENBERG
COLLEGE

EXC1801

July 31, 1995

Mr. James Wolfensohn
President
International Bank for Reconstruction and Development
1818 H Street, N.W.
Washington, D.C. 20433

Dear Jim:

You can imagine my excitement and good will when I heard that your chances to go to the World Bank were excellent and then they were realized. You have always done well and now you have a chance to do well for the world. It comes to few men.

An old friend, who possesses one of the most brilliant economic minds I have ever known, has written a lengthy document about the beginning of capital markets in developing countries. I asked him to synthesize it in a few pages, because I did not think you could read the tome. He has done this and it is enclosed. After you look it over, if there is a responsible official at the bank who would like to pursue it, I'll make the arrangements for a meeting. In the meantime, my very best, as always.

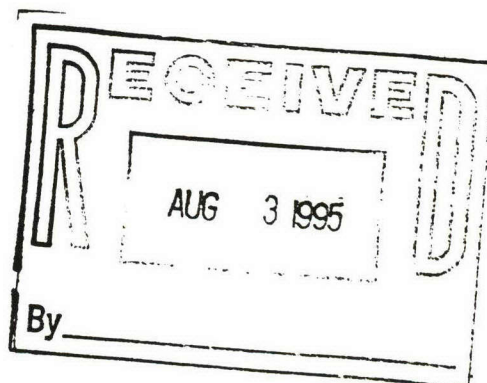
Sincerely,

Arthur
Arthur R. Taylor

ART:mo

Enclosure

OFFICE OF THE PRESIDENT
Michael B...
(or anyone)
DEC
Does anyone know about this
man: C. Klemmman
1/11



Prof. David T. Kleinman, Ph.D.
Financial and Economic Consultant

Box 1593 Cathedral Station
New York, N.Y. 10025
(212) 222-2244

MEMORANDUM

To: Mr. Arthur R. Taylor

From: David T. Kleinman

Date: July 19, 1995

The report that I prepared for the Brazilian Government and USAID in 1969 outlined the first plan for creating a capital market for debt and equity securities for a developing country undergoing hyperinflation that was ever implemented in an LDC. Its initiation and financing was undertaken in Brazil by the IFC, USAID and the Brazilian Government.

The goal of the plan was to introduce and develop rapidly a capital market in LDC's suffering hyperinflation. The essential purpose was to construct a capital market mechanism which would mobilize domestic savings that could make available to both the private and public sectors long-term capital, very scarce in countries undergoing high inflation rates.

The basic elements of the plan involved: (1) an inflation indexing system that would provide both investors and users of credit with a credible measure of the real cost of capital; (2) a market mechanism that would provide high liquidity for newly floated securities and which would make possible the rapid creation of a ready market for them; (3) the establishment of financial intermediaries (underwriters, market makers, etc.) that would

initiate and develop the market by creating the various appropriate financial instruments and then trading them throughout their lives; and (4) the diverting of seekers of long-term capital away from public sources (governments and international development institutions), through the newly established capital markets and their financial intermediaries, and ultimately to domestic savers-investors.

The implementation of the plan enabled local entrepreneurs to raise long-term debt capital (and equity) in spite of high rates of inflation. Shortage of long-term capital has been one of the most significant reasons for a slow rate of development in LDC's. At the same time, the appearance of debt instruments yielding a positive indexed real interest, drove many local entrepreneurs to repatriate their flight capital from abroad. Ultimately, these new securities also attracted foreign investors and overseas funds.

The new capital market accelerated economic growth by increasing substantially the volume of long-term investment capital to both the public and private sectors. It also contributed to a much more efficient allocation of the country's resources. This new market allocated financial (and therefore all other) resources to the most efficient economic sectors and enterprises, and thereby increased output, reduced costs of production and prices. It thus acted as an anti-inflationary force. Moreover, the new market for long-term indexed debt instruments diverted seekers of long-term capital away from pressing the government for such capital (governments being the only sources likely to accept negative

real interest rates caused by a lack of indexation for inflation). Such pressure usually resulted in inflationary printing of new money. Instead, the new capital markets, now yielding higher real returns, could mobilize investment capital from domestic savers, and at the same time induce the repatriation of flight capital, both anti-inflationary developments. Furthermore, governments would now be able to resort to their own domestic capital markets to borrow long-term (and other) funds, instead of printing new money, to cover a portion of their deficits. This would also have an anti-inflationary impact.

Thus, this new capital market would cause the return of flight capital, increase investments and accelerate economic growth. It would also contribute to more efficient allocation of savings (and other scarce resources) and substantially reduce the inflation rate.

In the summer of 1972, a Congressional committee held hearings about a model, submitted by me, for linking this new capital market to the major international capital markets. Once equity and debt securities began to trade in domestic LDC's financial markets, with debt securities indexed for inflation, it became possible and often advantageous for foreign investors as well to purchase them. This proposal has largely been realized in the past ten years. It has led to massive flows of foreign portfolio investments into LDC's. In that proposal, I suggested that portfolio inflows would initially only supplement loans from international development institutions, but eventually could replace them entirely. In fact, in recent years a great deal more money reached LDC's through

portfolio flows than through loans from international development institutions.

The recent Mexican peso crisis has shown that in addition to the establishment of LDC's capital markets and linking them with the major international financial centers and capital markets, it is important to devise mechanisms that would minimize sudden massive losses of reserves and sharp declines in exchange rates when managers of "hot" money decide to shift their funds away from LDC's. The international development institutions may want to consider a variety of measures to reduce such risks.

At times of crisis such as last December, the international development institutions may elect to extend margin credit, indirectly or directly, to dealers and market-makers in LDC's securities. When advanced to dealers outside LDC's, it would induce them to increase their inventories. Thus, fewer securities would be returned to LDC's for redemption at a loss in central bank reserves and causing a decline in exchange rates. The Fed has also at times resorted to changes in securities' margin requirements to avoid extreme fluctuations in market prices. The finding of optimum measures that would prevent or ease crises such as Mexico's is a major contemporary challenge in development finance.

The limited resources available to international development institutions will cause the latter to weigh the possibility of transferring some of their functions to the international commercial and investment banks. Using their scarce resources to increase liquidity for securities of emerging markets, inside LDC's

as well as outside them, and providing incentives to lengthen their maturities, would aid the international development banks to substantially leverage their impact. These are only a few of several initiatives that come to mind that might enhance the impact and effectiveness of the international development banks.

THE WORLD BANK/IFC/M.I.G.A.

OFFICE MEMORANDUM

DATE: August 17, 1995

TO: Mrs. Farida Khambata, CCMDR
Mr. Gary Perlin, FSD

FROM: Kate Oram, Executive Assistant, DECVP



EXTENSION: 31107

SUBJECT: RE - Correspondence from A. Taylor to Mr. Wolfensohn (EXC-01801

The attached from EXC was sent to Mr. Bruno for action. However, we think it should more appropriately have been sent to you. We would appreciate it if you could comment directly to Maree Aniba in EXC, if possible by the due date August 21st.

Many thanks.

cc: Maree Aniba

0235

Correspondence Management for the President's Office
CHORUS
External Correspondence Profile

Reference #: EXC-01801

For Action: Michael Bruno VPU: Room #: Telephone:	Log Date: 08/03/95 05:08:17 PM Status: Open Response Date:
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Correspondence Description:

From: Arthur R. Taylor, Muhlenberg College To: Mr. Wolfensohn Dated: 07/31/95 Topic: sending article from Dr. David Kleinman

Action InstructionsDue Date: ~~08/11/95~~ 08/21/95

4. Please review and advise.

Special Instructions

personal mail. JDW wrote a note to Michael Bruno (or anyone!) and DEC "Does anyone know about this man and his work i.e., Kleinman." dated 08/11/95.

Information Copies:

Please return to: Maree Aniba, EXC, E1227, 84138

*c c - Bruno
Chokri
MMB*

JAMES D. WOLFENSOHN

1818 H STREET, N.W.
WASHINGTON, D.C. 20433
Phone: (202) 458-5120
FAX: (202) 522-3433

May 22, 1995

Mr. David Woodward
74A, Fortescue Road
Colliers Wood
London, SW19 2EB
United Kingdom

Dear Mr. Woodward:

Thank you for your letter of May 2, 1995 and for your congratulations on my appointment as President of the World Bank.

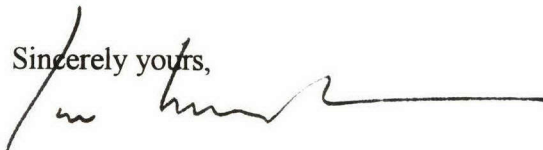
As you no doubt know, I don't take office until June 1 so at this point it is difficult for me to respond in detail to the concerns raised in your letter regarding the objectivity of World Bank research. That said, I would like to make two points:

First, I understand that research emerging from the World Bank is usually subject to both internal and external review. This is designed to ensure that the work fully meets the standards of the profession. Of course, the system may not function well, or may not function well for all products, and this is certainly something I will investigate

And second, much of the World Bank's research is empirical. And, again as far as I understand it at this point, the evidence underlying the Bank's research conclusions is routinely made available. This allows others to draw their own conclusions which, of course, need not correspond to those of the Bank.

These comments may go some way to allay your concerns. But let me add that I will look into this matter further when I have taken office. Thank you for your interest in the World Bank.

Sincerely yours,



James D. Wolfensohn

74A, Fortescue Road,
Colliers Wood,
London,
SW19 2EB.

613

2 May 1995.

Mr J. Wolfensohn,
President,
The World Bank,
1818, H Street, NW,
Washington,
D.C. 20433,
U.S.A.

Dear Mr Wolfensohn,

First of all, may I congratulate you on your appointment as President of the World Bank. As I am sure you appreciate, the World Bank's role in economic policy (and in an ever-increasing number of related areas such as health and education) in the developing world makes the Bank central to the future of much of the World's population. I wish you every success in what must be one of the most challenging positions.

My main purpose in writing to you is to draw to your attention to a particularly worrying feature of the Bank's activities in recent years, namely the **lack of objectivity in many of its publications, particularly with respect to the effects of adjustment policies**. I hope that you will be able to address this issue as a matter of priority.

The Bank's support for structural adjustment as a general strategy for developing countries has been, in effect, a global experiment. It is an experiment in that it was introduced, not on the basis of empirical observation of the effects of alternative policy régimes in developing countries, but on economic theories which were developed in and for developed countries. It is global in that its widespread application inevitably affects the economic environment of all countries, developing and developed, adjusting and non-adjusting, in addition to the effects of policy changes on the individual country which implements them.

The problem of a global experiment is that its results are, by definition, impossible to measure, because we have no other world with which to compare it. The most we can hope for is a rigorous and objective analysis of what happens *during* the experiment. The Bank has not merely failed to provide this; it has also acted in such a way as to subvert its provision by others. In some instances, this may have been unintentional, or the result of misplaced priorities among over-zealous staff members. In other cases, it is difficult to avoid the conclusion that this has been a deliberate policy by the Bank.

In this last category, I would include the use of the Bank's considerable research output, not to provide objective analysis, but to defend the Bank's current policies. This has been done, for example, by the uncritical use of data which are known to be unreliable (e.g. on infant and child mortality rates); the use of insensitive analytical methods to assess the social impact of adjustment; the failure to acknowledge factors which distort results in favour of adjustment (e.g. adverse selection); and the comparison of entirely non-comparable groups of "adjusting" and "non-adjusting" countries (e.g. health expenditure in the 1993 *World Development Report*).

[For detailed analyses of various World Bank publications, see:

David Woodward: *Debt, Adjustment and Poverty in Developing Countries*. London: Pinter Publishers/SCF(UK), 1992 (particularly Volume I Annex II).

Anthony Costello, Fiona Watson and David Woodward: *Human Face or Human Façade? Adjustment and the Health of Mothers and Children*. London: Institute of Child Health, 1994 (particularly Part I Sections 5 and 8).

Paul Mosley and John Weeks: "Adjustment in Africa". *Development Policy Review* 12(3):319-327, September 1994.

Paul Mosley, Turan Subasat and John Weeks: "Assessing 'Adjustment in Africa'". *World Development*, forthcoming.]

Clearly, it would be possible to ascribe these shortcomings to incompetence rather than deliberate distortion. However, my experience of World Bank staff members (mainly as a technical assistant to the British Executive Director in 1986-8) suggests that this is highly unlikely. Also, the probability of such incompetence so consistently favouring the current approach to adjustment must be remote. Moreover, even ignoring the analytical problems, the conclusions drawn are not uncommonly so distant from the data on which they are ostensibly based as to be little short of misrepresentation. This can only be deliberate.

In other respects, too, the Bank seems more interested in defending its policies and promoting its public image than in learning the true effects of adjustment. Major Bank publications (e.g. the *World Development Report; Adjustment in Africa*) are used to promote the Bank's position, and virtually ignore contrary views. The (remarkably brief) discussion of structural adjustment and health in the 1993 WDR is a case in point: all but one of the references given appear to have been written by current or past World Bank staff members or consultants; the other one (my own book) was added only after I had pointed this out in my comments on the draft version, and no account was taken of its contents.

The Bank's relations with NGOs also give some cause for concern in this regard. Over recent years, the Bank has put considerable effort into developing its relations with NGOs, both through consultation and by using them as implementing agencies. In some respects, this is no doubt welcome. However, it has created some degree of dependency; and the Bank has on more than one occasion sought to exploit this to circumscribe or discourage criticism. I would cite two examples: the threat to curtail access to World Bank information for two NGOs which produced reports critical of the Bank last Autumn; and an informal attempt by a senior member of the Bank staff to dissuade an NGO which was undertaking research on adjustment from challenging the basic tenets of the current approach.

I am sure you will agree that the objectivity or otherwise of the Bank's research is a critical issue, not only for the Bank itself, but also for the developing world. I hope you will also be persuaded by the sources cited above that there is a very real question mark over the Bank's current role in the analysis of structural adjustment.

Among the issues which need to be addressed are:

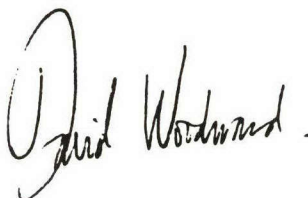
- whether recruitment procedures tend to bias the balance of Bank staff towards a particular view (specifically a neoliberal view) of economic issues;
- whether promotion policies and staff allocation (e.g. the marginalisation of dissenters) produces an incentive structure which artificially promotes the presentation of particular views in research and other publications;
- whether the "quality control" procedures for Bank research results in critical findings not being published, or being issued only in low-profile formats (e.g. internal working papers);
- whether the editing process distorts research findings, or imparts a bias to other publications;
- whether selection procedures, contractual terms, etc. for consultants encourages them to produce findings which they perceive as being what the Bank wants to hear;
- whether the Bank as an institution, or individual staff members, are abusing their position of influence with respect to NGOs and/or academic institutions in such a way as to promote research agendas favourable to Bank policies, or to discourage the development and dissemination of criticisms; and
- whether the terms of reference of the Inspection Panel should be extended

to include the Bank's research, or whether a similar body should be established for this purpose.

I would regard this issue as one of the most important facing you as in-coming President. If the Bank is indeed using its position to promote preconceived policies, reckless of their effects on developing countries and their people, this can only be described as irresponsible, and clearly contrary to the Bank's professed mission for the sustainable reduction of poverty. As a newcomer to the Bank, I hope that you will neither feel obliged to justify its past record, nor be so absorbed in its institutional culture as to accept its prevailing orthodoxy uncritically. Your appointment offers a real opportunity for the Bank to contribute to development and poverty reduction. I hope that you will feel able and willing to take it.

With all best wishes for the challenges ahead,

Yours sincerely,

A handwritten signature in dark ink, reading "David Woodward". The signature is written in a cursive, flowing style with a large initial "D".

David Woodward

005-8

THE WORLD BANK GROUP

ROUTING SLIP		DATE: June 1, 1995	
NAME		ROOM. NO.	
M. Bruno		S 9035	
☐	URGENT	☐	PER YOUR REQUEST
☐	FOR COMMENT	☐	PER OUR CONVERSATION
☐	FOR ACTION	☐	NOTE AND FILE
☐	FOR APPROVAL/CLEARANCE	☒	FOR INFORMATION
☐	FOR SIGNATURE	☐	PREPARE REPLY
☐	NOTE AND CIRCULATE	☐	NOTE AND RETURN
☐		☐	
RE: Correspondence sent out by Mr. Wolfensohn			
REMARKS: For your information			
FROM Maree T. Aniba		ROOM NO. E 1227	EXTENSION 84138

