Folder Title:	Board Actions - Brandt Commission - Board papers 01
Folder ID:	1770707
Series:	Board [of Executive Directors] Actions files
Dates:	02/01/1980 - 05/31/1980
Sub-Fonds:	Records of President Robert S. McNamara
Fonds:	Records of the Office of the President
ISAD Reference Code:	WB IBRD/IDA EXC-10-4548S
Digitized:	7/7/2021

McNamara Papers

Board actions
Brandt Commission 1980 (Jan - May)

BRANDT COMMISSION: STATUS OF PAPERS

CONFIDENTIAL

Proposal	Primary Responsibility/Author(s)	PPD	Date of Submission to: President	Board	Status
1. Expand Program Lending by the Bank (p. 291). /a	Stern	King	Done	Done	Board Memo R80-17(IDA/R80-22) of 2/5
2. Provide for greater co-financing by the Bank (pp. 256, 278).	Baneth	Jacob	Done	Done	Board Memo R80-22(IDA/R80-28) of 2/19
3. Abstain from imposition of political conditions on operations of IFIs (p. 291).	Benjenk	Ozgediz	Done	Done	Sent to Board May 30; discussion postponed indefinitely (R80-145).
4. Plan to effectively utilize the increased borrowing capacity of the Bank resulting from the doubling of its capital (p. 291).	Rotberg/Hittmair/Uhrig	Jacob	10/31	t.b.d.	A paper on borrowing prospects which also addresses the Brandt Commission proposals is being drafted.
5. Change the Bank's present "gearing ratio" /b so as to raise its lending capacity (p. 291).	Qureshi/Wood/Applegarth	Hicks	t.b.d.	t.b.d.	Paper being drafted.
6. Develop an action program to reduce absolute poverty in the poverty belts of Africa and Asia during the 1980s (p. 282).	Stern/Haq	Chernick/Burki	Done	10/15	Revised draft sent to Mr. McNamara for approval.
7. Analyze the likely debt and debt servicing problems in various categories of LDCs and the capacity of existing private and public institutions to meet these needs (p. 292).	Qureshi/Wood/Haq	Hicks	Done	Done	Sent to Board on September 18, 1980 (R80-285).
8. Define the role of the surplus countries in financing the adjustment problem of developing countries (p. 239).	Qureshi/Wood/Ikram	Hicks	Done	t.b.d.	Revised draft sent to Mr. McNamara on Aug. 8, 1980. Mr. McNamara has not yet cleared the paper for wider distribution.
9. Substantially increase Bank financing for exploration and development of energy resources (p. 292).	Stern/Rovani	King	Done	Done	Paper entitled "Energy in the Developing Countries" discussed by the Board on Aug. 5, 1980 (R80-206).
10. Use the Bank's guarantee to improve access of developing countries to capital markets (p. 292).	Qureshi/Wood/Ikram	Hicks	Done	Done	Sent to Board on July 15, 1980 (R80-208).
11. Develop an action program to increase food output in low-income, food-importing developing countries during the 1980s (p. 280).	Baum/Yudelman/Donaldson	Hicks/King	Done	Done	Sent to Board on September 26, 1980 (R80-294).
12. Provide greater participation of LDC staff in Bank management (p. 275)	Pollan/Rohrbacher/Jennings	Ozgediz	10/31	t.b.d.	Discussed by Personnel Management Committee on Aug. 5, 1980, and being revised to incorporate comments made at that meeting. PPR to work with Personnel Management on the revision of the paper.
13. Set up a new institution for exploration and development financing for non-fuel minerals (p. 292).	Stern/Baum/Fuchs	King	Done	Done	Sent to Board August 14 (R80-249).
14. Provide greater decentralization of the management of the Bank's operations (p. 275).	Wood/Burki	Ozgediz	3/15/81	3/31/81	Paper to be drafted by Wood in collaboration with PPD and OPD. Draft now scheduled for management review in March 1981.
15. Provide borrowing countries a greater role in the decision-making process in the Bank (p. 275).	Nurick/Thahane/Golsong	King	t.b.d.	t.b.d.	Golsong's draft received. Discussed by Haq/Burki with Thahane. Preparation of the paper postponed till after the Annual Meeting.
16. Examine the possibility of the Bank's refinancing export credits for capital goods (pp. 234-235).	Qureshi/Ikram	Jacob	10/30	11/11	Paper on options being prepared by P&B in collaboration with IFC.
17. Consider the creation of a new international financial institution - a World Development Fund - to supplement existing institutions and to diversify lending policies and practices (p. 252)	Qureshi/Haq	Burki	12/15	1/14/81	Paper to be written after the completion of other papers. This paper may have to slip since some of the more important inputs are being delayed.
18. Brandt Commission Proposals of Relevance to the World Bank: Progress Reports for the Development Committee					
First Progress Report	Haq/Burki	Ozgediz	Done	Done	Discussed by Board on Aug. 26, 1980 (R80-234).
Second Progress Report	Haq/Burki	Ozgediz	3/1/81	3/15/81	

/a References are to page numbers of the Brandt Commission Report.
/b The ratio of receivables to capital, as prescribed by the Articles of Agreement.

Notes: Dates in parentheses indicate previous schedule.
t.b.d. = to be determined.

Policy Planning Division
Policy Planning & Program Review Department
October 3, 1980

A

FOR EXECUTIVE DIRECTORS' MEETING

For consideration on March 18, 1980

R80-17
IDA/R80-22

FROM: Vice President and Secretary

February 5, 1980

LENDING FOR "STRUCTURAL ADJUSTMENT"

Attached is a memorandum entitled "Lending for 'Structural Adjustment'" dated February 5, 1980, from the President.

Questions on this document may be referred to Mr. Stern (extension 72004) or Mr. Haq (extension 60121).

Distribution:

Executive Directors and Alternates
President
Senior Vice President
President's Council
Vice Presidents, IFC
Directors and Department Heads, Bank and IFC

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

Office of the President

February 5, 1980

MEMORANDUM TO THE EXECUTIVE DIRECTORS

SUBJECT: Lending for "Structural Adjustment"

Introduction

1. The changes in the international economy in recent years, including the increase in the price of oil, continued high levels of inflation and prolonged period of slow growth in the OECD countries, are posing increasingly acute problems for many of the developing countries. The management of their economies has become more complex. They face deteriorating terms of trade and growing current account deficits. With increasingly severe resource constraints governments must consider how they can adjust their development patterns and economic structures to the substantially changed international economic environment. This set of circumstances has led to considerable discussion of additional ways and means by which the Bank can assist its members, including the use of a new form of lending which we have named "structural adjustment" lending.

2. In preparation for the meetings in Belgrade, we discussed the possibility of lending to assist countries which were prepared to undertake a program of adjustment to meet an existing or to avoid an impending balance of payments crisis. Subsequently, this possibility was discussed in the Development Committee and in the Annual Meeting. Such lending has several distinguishing features. First, it will be a fundamental instrument for the dialogue between the Bank and the country on various aspects of development policy and on the nature and scope of change to be supported. Second, it will provide finance over a number of years in direct support of specific policy reforms. Third, it would provide foreign exchange to finance imports not linked in advance to specific investment programs. Such loans would therefore disburse quickly - a feature of particular interest in view of the current account prospects for the next several years.

The Short-Term Prospects

3. The analysis of the prospects facing the developing countries in the next several years is not yet fully refined, but the initial assessment clearly indicates that the current account deficits will be very large and

that growth rates will be much smaller than previously anticipated. The current account deficit of the oil importing developing countries, associated with a per capita GNP growth of 2.3%, is now estimated at US$74 billion for 1980 and it is expected to rise further in 1981 and 1982. This compares to a deficit of US$26 billion in 1978. As a share of GNP, the current account deficit of the low income countries in 1980 is estimated at 4.7%, compared to 3.5% in 1975 and to 1.4% in 1973. For the middle income countries it is estimated at 4.8% of GNP, slightly less than their 1975 ratio of 5.5% but substantially higher than the 0.9% of 1973.

4. There are many reasons for this increase. Obviously the increased price of oil is one factor. Other factors contributing to the increased current account deficit include the slowdown in economic growth of the OECD economies and the impact this has on both the volume and the price of LDC exports, as well as the continued high rates of inflation which affect the cost of imports. Many of the changes are permanent or long-term in character and will require long-term structural adjustments in the economies of the developing countries. These adjustments should be designed to reduce the current account deficits to more manageable proportions -- a reduction of perhaps 50% -- within five to seven years. However, during the transition period the increased deficits will require substantial additional financing on a medium to long-term basis. The low income countries which lack access to the private capital markets can only finance their deficits through increased ODA. Should ODA be inadequate, a further reduction in their already low rate of growth would be the inevitable result. Many of the middle income countries have had access to private capital but the debt accumulated since 1974 has reduced their ability to borrow and may have limited the willingness and the ability of the commercial banks to lend.

5. The relatively short-term finance available from the commercial banks and the resources available from the IMF to the developing countries for the financing of the adjustment process need to be supplemented, both in amount and maturity, if the debt problems of many of the countries are not to assume serious dimensions. "Structural adjustment lending" by the Bank can be a means to serve these needs.

6. We anticipate substantial demand for structural adjustment lending from countries in acute balance of payments difficulties and from countries with programs of adjustment which will require support if more acute difficulties are to be avoided.

7. While the likely amount of such lending available from the Bank will be small compared to the total amount of external capital required, the Bank's initiative may encourage the provision of similar assistance from other sources to those countries which are seen to be implementing appropriate policy reform measures. We expect that there will be opportunities to cofinance our structural adjustment loans with both official and private sources of finance but, more important in terms of volume, we expect that sound programs of structural adjustment, acceptable to the Bank as a basis for lending, will encourage bilateral aid agencies to expand lending for this purpose and complement and sustain lending from commercial banks for general purposes.

FOR OFFICIAL USE ONLY

The Characteristics of "Structural Adjustment" Lending

8. Lending for "structural adjustment" is only justified if there is a specific program of structural adjustment to be supported which has as its objective increased efficiency of resource use and improved responsiveness of the economy to changes in economic conditions. The nature of such programs can only be determined in the country context and may vary widely. In many cases it will involve a reassessment of the medium-term investment program to bring it in line with a changed availability of investable and budgetary resources. The composition of the investment program may also have to be altered by, for instance, reducing investment in projects with long gestation periods and emphasizing investments which will yield results more quickly and those which have a greater employment effect. Frequently, the program will also involve the country's trade regime. For example, for countries which rely heavily on a few primary commodities for exports, diversification as a basis for expansion will be important. This may require incentives for investment in non-traditional exports, either agricultural or industrial, a revamped marketing effort and investment in transport and distribution. For countries whose industries have developed behind high levels of protection and therefore, have failed to realize their export potential, it may be appropriate to move to more uniform and moderate levels of protection to eliminate the distortions and to make such industries more internationally competitive. This may involve assistance to such industries to finance complementary investment and to redesign product lines. In other instances, it may be desirable to reorient investment to domestic markets to stimulate growth and reduce imports in the face of limited exports prospects. Programs of structural adjustment may also involve issues of domestic resource mobilization, price incentives or the efficiency of resource use. While it is impossible to specify the components of such a program, their common objective would be to reduce in the medium-term, say five to seven years, the current account deficit to a sustainable level as a percent of GNP.

9. Such programs of "structural adjustment" are neither simple to formulate nor easy for governments to decide on. In many cases assistance from the Bank, and the IMF, will be required. We are prepared to make staff and consultants available, wherever necessary, to assist governments in this process. Internally we shall have to reorient our economic and sector work program to strengthen our capacity to advise governments on their programs of structural adjustment and to evaluate such programs for lending purposes.

10. Once the objectives and main directions of the necessary structural adjustment are decided on by the country, the implementation is likely to take several years and results will be seen only gradually. For instance, a decision by the government to reduce the level of protection and make it more uniform is only a first step. Specific actions on tariffs, quantitative limitations, investment incentives, and financial support can only be decided on the basis of industry studies which may take one to two years to complete. In some countries restructuring of production and marketing strategies of public sector industries might be involved. Thus lending

for "structural adjustment" must be conceived as an association with a borrower in a program of structural change over three to five years which will require financial support and technical collaboration throughout this period. Because lending for "structural adjustment" provides support for an evolving program, it will be important to be specific about the medium-term objectives of the government at the outset. However, policy decisions and other implementation action to be taken in the period covered by the loan should also be specified, so as to permit the borrower and the Bank to monitor progress during the period both on the immediate actions agreed to and toward the longer term objectives. Loans for structural adjustment usually will cover a 12 to 18 month period. It is desirable therefore to provide for at least one review of progress during that time. Subsequent loans needed to support the multi-year program would be based on satisfactory completion of the actions previously agreed to, confirmation or amplification of the medium-term objectives, and an additional program of specific actions to move further toward those objectives.

11. It is clear that lending for structural adjustment will only be possible where a government has accepted the need for such adjustments and is prepared to collaborate with the Bank in a review of its policies and the formulation of a program. The Bank could not, nor would it wish to, impose its views as to what constitutes an appropriate program. Lending for structural adjustment will only succeed if the program to be supported represents a firm government decision based on an intensive analysis and dialogue, in which the Bank can participate to whatever extent the government desires. To be successful, the program which emerges should be feasible from all points of view: politically, administratively and economically.

Collaboration with the IMF

12. Since lending for structural adjustment would normally address macro-economic policy issues related to the balance of payments, the need to consult the IMF is readily apparent. Since the last Executive Board review of program lending in April 1977, Fund staff have cooperated closely in processing program loans. In several cases a Bank staff member joined the Fund consultation or review team (e.g., Turkey, Jamaica and Guyana). In other instances, the Bank's program loan appraisal mission overlapped with the Fund's consultation or review mission in the field (e.g., Sudan and Zambia). It is normal practice for the Bank and the Fund staff to consult each other closely in Washington and share information and views. The Bank usually regards the success of the short-term economic stabilization or recovery program (on which the IMF standby arrangements are based) as important for the fulfillment of a government's medium-term investment or development program. For its part, the IMF relies on the Bank's judgements on the appropriateness of a country's medium-term investment program which provides a context for stabilization measures and is particularly relevant to Extended Fund Facility (EFF) programs.

13. Lending for structural adjustment should be viewed as complementary to the Fund assistance, although it will differ in type and scope of policy measures to be agreed to and in the time frame for assessing the impact of structural reform policies to take effect. Thus, a situation may arise where an EFF operation is mounted by the IMF in a country and a parallel loan for adjustment assistance is provided by the Bank to support a set of specific policy measures aimed at long-term structural adjustment.

14. As lending for structural adjustment expands, it will be essential that the coordination with the Fund be effective. We will ensure that there is a regular exchange of information on plans for assistance and seek to expand participation in the appropriate missions.

Prospects for Lending for "Structural Adjustment"

15. The need for such lending is great as indicated by the aggregate projections. However, the extent of lending for structural adjustment will depend not on the magnitude of the current account deficit of the developing countries but on the number of countries which are prepared to formulate programs of structural adjustment and the speed with which satisfactory programs can be developed. A loan for Kenya will be circulated to the Board shortly and discussions are at various stages with the Philippines, Turkey, Bolivia, and Tanzania. Exploratory talks have been held with a number of other countries. We expect that these discussions will yield specific proposals to be placed before the Executive Directors during 1980. Undoubtedly, additional proposals will emerge in the course of the year as the balance of payments difficulties, immediate or impending, in individual developing countries are identified more clearly and governments begin to deal with them. It is therefore not yet possible to be precise about the amount of lending for "structural adjustment" or the extent to which it may affect the Bank's lending program.

Robert S. McNamara

B

International Bank for Reconstruction and Development
International Development Association

FOR OFFICIAL USE ONLY

FOR EXECUTIVE DIRECTORS' MEETING

For consideration on
March 11, 1980

R80-22
IDA/R80-28

FROM: Vice President and Secretary

February 19, 1980

WORLD BANK COFINANCING

Attached is a memorandum entitled "World Bank Cofinancing" dated February 19, 1980, from the President.

Questions on this document may be referred to Mr. Baneth (extension 75837).

Distribution:

Executive Directors and Alternates
President
Senior Vice President
President's Council
Vice Presidents, IFC
Directors and Department Heads, Bank and IFC

FOR OFFICIAL USE ONLY

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

DECLASSIFIED
AUG 04 2014
WBG ARCHIVES

Office of the President

February 19, 1980

MEMORANDUM TO THE EXECUTIVE DIRECTORS

SUBJECT: World Bank Cofinancing

I. Introduction

1.1 The World Bank has been playing an increasing role in coordinating and stimulating external capital flows to its borrowers. It has done so through a range of activities of different degrees of intensity and formality. Cofinancing is the most formal type of role played by the Bank, in which World Bank funds are directly associated with funds provided by other sources in financing specific projects or programs in developing countries.1/ The number of IBRD/IDA cofinancing operations rose from about 10 per year in the late 1960s to 34 in FY73 and 107 in FY79, and is expected to reach about 130 in FY80. The volume of cofinancing, i.e., the amount of funds provided by the colenders, rose from $448 million in FY73 to $3,205 million in FY79, and may reach $7,000 million in FY80.2/ In FY79, 43% of the projects approved by the Board involved some cofinancing, and the funds provided by colenders were equivalent to 32% of total Bank lending. Though these amounts should be seen in the context of overall capital flows to developing countries, which are many times larger and have also grown rapidly, they are nevertheless substantial. Developing countries again face sharply increased resource requirements. Within the range of World Bank activities aimed at helping them surmount this problem, cofinancing can play a useful and perhaps increasingly important role. This is especially true with respect to the Bank's cooperation with private capital sources.

1.2 This memorandum reviews the Bank's recent experience with cofinancing operations and analyzes the main ways in which their volume and development impact might be enhanced. In general, the memorandum concludes that there are several practical ways in which the Bank can proceed with its efforts to expand its cofinancing role. It is worth noting at the outset, however, that the overall thrust of the proposals is to strengthen this activity in the near term and not to make radical changes in World Bank operations. This memorandum discusses past experience and new proposals separately for each of the three main categories of cofinancing partners, namely: official aid agencies, export credit institutions, and private lenders.

1/ Annex A contains definitions and terminology relating to cofinancing.

2/ Attachment 1 shows the breakdown of cofinancing by source for the period FY73-79. In the first four months of FY80, actual cofinancing was about $2,300 million.

1.3 One factor common to all cofinancing operations is the set of services the Bank offers to confianciers in sharing with them the benefits of its project preparation, appraisal and supervision procedures. These services are not cost free. The Bank incurs the cost of the additional staff time spent on cofinanced projects and rarely receives similar services in return. It is not yet possible to calculate these additional costs accurately, but it has been estimated that cofinancing increases a project's appraisal costs by 5% to 10% and supervision costs by about 20%. Naturally when the Bank funds released by cofinancing are used for other projects, the new projects also add to the Bank's overall administrative costs. Some other services rendered to specific cofinanciers such as acting as billing agent, also entail costs. These costs are modest in comparison with the benefits of cofinancing, which accrue to Bank borrowers as a group, both those which receive cofinancing directly, and those which receive the Bank resources released by it. It is therefore appropriate that these additional costs should be borne by the borrowers collectively, that is by the Bank itself.

II. Cofinancing with Official Agencies

2.1 Throughout the period FY73-79 official agencies provided around 60% of the total cofinanced funds, and participated in 70% of cofinancing operations. Until 1975, these were almost exclusively DAC agencies. Following the oil price rise in 1973-74, official aid from OPEC sources rose dramatically. The Bank then had an opportunity to assist both the oil-importing developing countries and relatively new OPEC development institutions, which wished to accelerate the commitment of their funds through cofinancing, and thereby benefit from the World Bank's project preparation, appraisal and supervision experience. OPEC sources accounted for over half of the Bank's cofinancing with official sources in FY75 and FY76.1/

2.2 These efforts may have secured some increases in aid pledges. The main benefit from the Bank's cofinancing, however, was to increase the effectiveness of their aid and hasten its commitment to specific projects. Because of earlier commitment, disbursements were also advanced, even if the disbursement process itself may not always have been accelerated. In subsequent years, the share and even the absolute amount of cofinancing with OPEC sources fell, as these agencies built up their own staffs and procedures.

2.3 In some cases, the Bank has also helped to accelerate the utilization of aid from DAC members. However, most cofinancing with DAC aid agencies has been motivated by a mutual will for coordinated approaches and by a desire to spread aid activities over many countries and sectors.

1/ Including national government agencies and multilateral institutions deriving their resources wholly or largely from OPEC members.

Such spreading of aid activities may by itself entail a cost, particularly for small borrowers, in confronting their small administrations with an array of external agencies. However, given the political and other motives for spreading aid to several countries and sectors, cofinancing reduces the administrative burden on the borrower. Furthermore, cofinancing activities can benefit from the considerable country experience and large technical assistance resources of some bilateral aid agencies.

2.4 Cofinancing with the World Bank can also reduce or eliminate the procurement disadvantages of tied aid financing. This is done in a particularly effective way when several aid agencies participate, and tied aid does not have to finance supplies for which the aid agency's country is an inefficient supplier. The Bank facilitates this by combining cofinancing from many appropriate sources. Thus in FY78, the Madagascar Power Project was financed by IDA and six aid agencies. The complementary credit for Tarbela in Pakistan, also in FY78, brought together IDA and seven aid agencies.

2.5 On the whole, cofinancing with official aid agencies has worked well. It has helped to channel aid funds to high priority uses and it has been an increasingly active instrument of aid coordination. The qualitative impact of such coordination cannot be rigorously measured, but it is generally agreed that it has increased the developmental impact of aid by avoiding fragmentation and by saving scarce managerial time in the borrowing countries.

2.6 The renewed crisis faced by developing countries as a direct and indirect result of the latest oil price increase will again require extraordinary efforts by the international community, especially in meeting the needs of the poorest countries for sharply increased concessional assistance. There will be renewed needs and opportunities for the Bank to make a vigorous effort to reactivate and develop cofinancing arrangements with the aid agencies of oil-exporting countries. The pressures on developing countries will also intensify the need for efficiency and coordination of aid, and the Bank can continue to expand its joint activities with bilateral and multilateral aid programs originating in DAC member countries.

III. Cofinancing with Export Credit Institutions

3.1 In export financing, the Bank's partners are specialized agencies (like the US Export-Import Bank) and also ordinary commercial banks extending buyers' credits.1/ Official insurance or guarantee agencies (like ECGD

1/ In this paper no distinction is made between buyers' credits and suppliers' credits unless otherwise noted. Commercial banks also make direct "sovereign risk" loans, unguaranteed in the capital exporting country. These are discussed in Section IV on page 5.

FOR OFFICIAL USE ONLY

and COFACE) are important indirect participants, as are monetary authorities which refinance export credits on specially favorable terms. Cofinancing allows these agencies to participate in deals which they could not conclude alone, either because the loans would be too big or because their country's suppliers would be clearly unsuitable for substantial parts of the projects.

3.2 Cofinancing with export credits grew from $71 million in FY73 to $514 million in FY74 but has shown no clear trend since. At $652 million in FY79, cofinanced export credits were a little lower than in FY74 in real terms. During the same period, net disbursements of all export credits to developing countries rose from about $3.3 billion in 1973 to $13.2 billion in 1978.1/

3.3 Cofinancing with export credits can take the form of organized joint financing. In this, the Bank plays the central role in organizing and supervising the financing process, by arranging for export credit agencies to participate up to agreed amounts and on appropriate terms in the financing of a common list of goods to be procured under international competitive bidding. This procedure ensures competitive suppliers, but borrowers sometimes feel that it results in adverse financial terms. In recent years, unorganized parallel financing has been a more usual practice. The Bank and the borrower agree on dividing the project into separate packages. The borrower assumes full responsibility for negotiating export credits, and takes into account their availibility and terms in awarding the contract. Under this procedure, it is sometimes difficult to ensure that only the most competitive suppliers are selected. Yet cofinancing with export credits, when successful, has several advantages for borrowers: it ensures that this resource is applied to high priority projects and programs, it helps to reduce and even cancel the cost advantage of procurement tying, and the overall financial terms of export credits are often quite favorable.2/

3.4 In recent years, most export credits have been extended by commercial banks, insured by specialized agencies in the exporting countries and given access to specialized refinance facilities. In practice, commercial banks have generally found it easier to work without World Bank involvement, often complementing export credit facilities with straight financial credits for down-payments, local currency costs, or procurement in third countries. This is in part because it has been difficult to reconcile the Bank's procurement rules with those governing access to specialized insurance and refinancing facilities in the exporting country. These difficulties have also hampered efforts by the Bank and the borrowers to arrange coordinated financial packages for projects.

1/ Source: DAC. The commitments, of course, were much higher.

2/ Attachment 2 shows the terms of export credit cofinancing arrangements obtained for selected recent projects.

3.5 There is no easy solution to this problem. One possible approach might be to establish general lines of credit for individual borrowing countries to cover procurement on a range of projects, rather than arranging financing on a project by project basis only. With the prior authorization of export credit insurance agencies and monetary authorities, commercial and specialized banks would agree in advance to finance a certain proportion (possibly up to 100%) of procurement placed in that country on the basis of international competitive bidding. Once established, such arrangements would have administrative simplicity as well as the advantages of continued full adherence to efficient procurement practices, and might well enhance the volume and development impact of resource flows to developing countries. Provided such an agreement covers a high proportion of potential suppliers, it should be beneficial to all involved. Because of the many countries and types of agencies involved, considerable negotiating effort will be required. The Bank has started to consult with export credit agencies and commercial lenders as to their interest in such "umbrella type" arrangements, and proposes to pursue these efforts.

IV. Cofinancing with Private Sources

4.1 Perhaps the most dramatic change in development finance in the 1970s was the expansion of lending to developing countries by commercial banks. In terms of net annual disbursements, these grew from an average of $4 billion in 1970-72 to $10 billion in 1974, $20 billion in 1978 and an estimated $23 billion in 1979.1/ In 1974 and 1975, recycling of OPEC surpluses constituted the main source of these funds. In the following years, very liquid conditions dominated the international banking system, because of a combination of easy monetary policy in the US and weak credit demand throughout the OECD area. This allowed commercial bank lending to continue expanding after OPEC surpluses fell, and actually to reach its greatest growth rate in 1978 when the OPEC countries were overall net users rather than sources of commercial bank funds. This state of high liquidity of the banking system also created intense competition among banks, which in turn resulted in a narrowing of "spreads" charged over the basic cost of funds (the London Interbank offered rate, LIBOR, for six-month funds is the most widely used point of reference), lengthened maturities of loans, and greatly reduced differentials in the terms applied to developing countries and other borrowers.

4.2 In this environment of highly liquid markets, easily available loans and little discrimination between borrowers, neither borrowers nor lenders saw much benefit in cofinancing with the World Bank. The rate of growth in the volume and number of cofinancing operations has nevertheless been significant. There were three operations accounting for $136

1/ Source: OECD. Amounts exclude guaranteed export credits.

million in private cofinancing in fiscal years 74 and 75, and a total of 26 cofinancing operations accounting for $929 million in private funds over the following three fiscal years. In calendar year 1979, there were 18 cofinancing operations with commercial banks supplying $1353 million to 13 countries. However, these amounts are modest in comparison with the estimated $23 billion net lending to developing countries by commercial banks in 1979. Banks were so eager to lend to developing countries in the past few years that there is no indication that past cofinancing has added significantly to the flow of funds to the beneficiaries, or eased the terms on which such funds were available. The benefits of the Bank's cofinancing with private sources must be seen in their contribution to laying the groundwork for assisting developing countries secure continued access to international capital markets in the long run. As noted in paragraph 4.10 below, developing countries will need to continue and, in fact, increase their borrowing from commercial banks in the next few years. Yet broad economic and institutional factors will both make for much tighter credit conditions and create specific constraints on developing country borrowings from these sources. These new circumstances could make for a sharp further increase in cofinancing with the World Bank; more importantly they should enhance the value of such cofinancing in securing additional capital on reasonable terms. In formulating policies for maximising the Bank's usefulness in this new situation, it may be useful to review the Bank's procedures and experience to date.

Procedures and Experience

4.3 In contacts with commercial banks, regular operating staff are assisted by the Senior Adviser, Cofinancing, whose office was established in October 1975, and in the Latin America and Caribbean Region, by an adviser in the Regional Vice President's Office. The specialized cofinancing staff which is now reinforced by a special cofinancing unit in the Legal Department, initiates contacts with commercial banks and is a major focal point for continuing relationships with them. They inform lenders about the Bank's and borrowers' general policies and concerns, but for project-specific information, they refer them to the Regional Offices and to the borrowers. The specialized staff is also the Bank's original source of information and advice on the best sources of commercial financing for particular projects. In general, they actively promote cofinancing both with commercial banks and with borrowers.

4.4 Lenders may seek general information or be interested in a specific project listed in the "Monthly Operational Summary." The Bank then gives them broad, non-confidential information about cofinancing needs and possibilities, and facilitates contacts with the proper agency of the borrower. When mutual interest develops, potential cofinanciers can be given confidential documents, with the borrower's permission. Normally, the organization of the cofinancing arrangement will be quite advanced, and a lead bank will have been selected, before confidential materials, such as appraisal reports, are released to commercial banks.

4.5 When commercial banks extended untied financial loans as part of cofinancing with the Bank, the Bank generally includes a cross-default clause in its loan agreements. Cross-default clauses, a standard feature of commercial banks' international loans, link the loans of several lenders in such a way that a default on any associated loan is a default on all associated loans. The Bank has accepted optional cross-default provisions which give it the right, at its option, to exercise its remedies in the event that the cofinancier suspends or accelerates its loan as the result of a default under its loan agreement. Some private cofinanciers feel that this clause gives them additional security in that the Bank has the right to apply its remedies if default occurs on these loans. They often press for a removal or reduction of the optional character of the clause so as to increase its deterrent effect and its value to them. The Bank has refused to commit itself in advance to exercise its remedies in the case of a suspension or acceleration by the commercial banks on their loans. It has made it clear that it reserves the right to decide whether and in what way to take action in such a case. As for borrowers, they have shown some distaste even for optional cross-default provisions.

4.6 Past cofinancing operations of the Bank have not substantially increased the volume or improved the terms of commercial bank loans. In the prevailing easy market conditions, this was usually neither feasible nor particularly useful. However, the Bank has increased the market's base by introducing new lenders. This will help to protect the market against the emergence of problems affecting particular lenders, such as portfolio limits on lending to specific countries, insufficiency of the capital base, or limitations arising out of national monetary and balance of payments policies. This impact may be achieved even if after introduction of one or a few operations, subsequent loans are concluded without reference to the Bank. This has indeed happened occasionally.

4.7 Measured by this standard of diversification and given the limited interest for cofinancing due to market conditions, the Bank's role has been helpful. In particular, the Bank has had success in introducing new lenders to the market. In early years, US banks dominated private cofinancing sources. From about 50% in 1975 and 1976, their share dropped to 17% in 1978 and 32% in 1979, while the share of European banks increased from 18% to 27% over the same period.1/ The share of Japanese banks increased from 5% in 1975 to 35% in 1979. It is noteworthy that while overall Japanese commercial bank lending to developing countries contracted sharply between 1978 and 1979, cofinancing did not.

1/ These figures relate to calendar years.

4.8 In 1975, 14 commercial banks signed loans pertaining to cofinancing arrangements with the World Bank; in 1976, 20 did so, (of which only 6 were "repeaters" and 14 were new to this type of operation); in 1977, 58 (of which 46 new and 12 repeaters); in 1978, 19 (of which 8 new and 11 repeaters); and in 1979, 50 (of which 18 new and 32 repeaters). Thus 100 commercial banks have already made loans for cofinancing operations, many of them several times. "Repeater" banks' cofinancing loans have tended to increase over time. Relatively recent newcomers include both large banks e.g., Credit Agricole, and second-tier banks, whose involvement in international lending operations can give such markets greater depth and stability.

4.9 Most of the commercial banks cofinancing well-established international borrowers like Brazil and Argentina had already lent to those countries in recent years. In several other cases, however, most participants were making their first loan to the borrowers. For example, none of the six commercial banks which cofinanced the Pattani Hydroelectric Loan to Thailand, none of the six involved in the Second Livestock Loan to Romania, and only four out of the 19 participants in the Eighth Power Loan to Malaysia had previous relations with the country. Thereafter, five of the participants in the Thailand project, and five of the new participants in the Malaysia project undertook direct eurocurrency lending to those same countries.

Present Opportunities for Expanded Cofinancing

4.10 Developing countries now face a deteriorating economic environment. To mitigate the slowdown in their economic growth and facilitate their adjustment to the new economic environment, they need to incur and finance sharply increased balance of payments deficits. These cannot be financed without large private lending to them, in particular continued active lending by commercial banks. The effective recycling of the surpluses generated by the new oil price rise is also dependent upon such lending. Yet commercial bank lending will be constrained by a variety of broad economic factors, including competition from developed countries on capital markets, and the generally more restrictive monetary policies likely to prevail. More specific institutional factors will also constrain commercial bank lending to oil-importing developing countries. They include the increased share of such loans in the banks' portfolios, the relationship of these assets to the banks' capital, and the banks' risk-bearing capacity. Many of these factors are, in the ultimate analysis, related to uncertainties concerning the creditworthiness of developing countries and the soundness of their development. Cofinancing with the World Bank takes up an important new role in this context. Cofinanced loans are used for sound development projects and programs. By thus ensuring the soundness of the final assets, cofinancing can effectively contribute to bolstering the banking system and expanding its lending on a sustainable basis. It can also help to introduce assets best suited to the needs of specific types of banks and other investors.

4.11 There are three main opportunities for the Bank to play an expanded role in cofinancing with private sources. The first lies in the creative use of lending to finance structural adjustments; the second involves additional flexibility in terms and conditions of Bank loans; and the third is to assist borrowers in gaining access to private sources of long-term finance.

4.12 Structural Adjustment Loans. Such lending may form an increasingly important part of the Bank's efforts to help developing member countries adjust to structural problems. Cofinancing by commercial banks can increase the volume and development impact of such assistance. The very existence of structural adjustment problems would sometimes deter commercial bank lending. A structural adjustment loan signals that effective development policies are being followed, and co-financing with such a loan may be a particularly appropriate way to introduce or reintroduce commercial banks to that country.

4.13 Terms and Conditions of Lending. The Bank's present loan portfolio offers limited resale possibilities because it is made up of fixed-rate instruments. Given a choice between an IBRD bond and an unguaranteed World Bank loan to a developing country, lenders will normally prefer the bond unless the loan were priced to yield substantially more. The Bank can enhance prospects for sales of participations to the private sector by deliberately designing particular loans to include a portion for resale on terms other than those used for financing by the Bank itself, i.e., on floating rate terms. Both the Inter-American Development Bank and the International Finance Corporation do this regularly. While the volume of their operations is much smaller than the Bank's (IDB has arranged 14 such private cofinanced loans, for a total of $378 million, in the past four years), their experience indicates that this technique could offer a useful additional tool to be used by the Bank in selected cases.

4.14 In future, the Bank will actively explore the desirability of making part of its loans for selected projects in the form of floating rate medium-term loans, with the deliberate intention of reselling to private investors the instruments pertaining to these loans. Such resales would be arranged before, or at the time of disbursement, so that the Bank's lending authority will remain exclusively committed to long-term, fixed interest loans. The Bank could thus supplement its own resources by tapping the very large potential offered by short-term private capital funds. The number, variety and interest of cofinanciers should be increased by the loans having "passed through" the books of the Bank. All loan sales would be made without Bank guarantees or any other type of recourse to the Bank, and would leave unimpaired the Bank's further lending authority out if its own resources. This will be usually preferable to the use of other methods, such as firm "buy-back" agreements, which would involve some impairment of the Bank's future lending authority.

4.15 We think these and similar new arrangements could be attractive to some commercial banks and provide more assurance to colenders than the Bank's current cofinancing practices. We see no need to take the further step of making the exercise of the Bank's remedies mandatory in the event of defaults on colenders' loans, in connection with these or more traditional cofinancing operations.

4.16 Assistance with Long-Term Finance. In the 1950s and 1960s, several higher-income borrowers arranged for bond issues--both public and private placements--to complement World Bank loans in financing specific projects. Similar arrangements might be used to assist present borrowers in improving access to private sources of long-term finance. In 1978, World Bank borrowers issued over $4 billion worth of international bonds. Association with a World Bank project through cofinancing could add to the attractiveness of developing country bonds to certain investors. We plan to identify a limited number of projects suitable for such cofinancing, beginning with large projects related to sectors which relevant institutional investors are already financing in countries most likely to be successful in securing such private finance, and we shall consult with borrowers as to how the Bank might assist them. Such projects could then be simultaneously discussed with large insurance companies and pension funds operating on national markets (with respect to private placement), and with underwriters operating in interna tional markets (with respect to public issues of international bonds).

V. Conclusion

5.1 Cofinancing has grown rapidly in recent years. Through cofinancing arrangements with official aid agencies, export credits and commercial banks, the Bank has improved the development impact of external capital and increased the effectiveness with which tied funds are used.

5.2 The Bank has achieved some success in introducing new lenders to developing countries. However, while cofinancing with private sources increased substantially in recent years, this increase was only a fraction of the total increase in commercial bank lending to developing countries that took place over the same period. It is unlikely that much cofinancing with private banks was additional to capital flows which would have otherwise taken place, or that it materially affected the terms and conditions of such flows.

5.3 Over the next few years, competition for external capital is going to be more acute, in particular by developed countries. Monetary policies are likely to continue the restrictive, anti-inflationary stance they recently assumed, and thus reduce the liquidity of the world banking system and increase the cost of funds. Past borrowing, which has increased the share of developing country loans in the portfolios of commercial banks,

FOR OFFICIAL USE ONLY

will also make further lending to such countries increasingly difficult, particularly in view of the deteriorating capital structure of many banks. In these circumstances, cofinancing with the World Bank may play a much more important role. By ensuring the sound use of external capital and the overall effectiveness of development and structural adjustment programs, it can serve as the catalyst needed in critical cases for private capital inflows to occur, on reasonable terms.

5.4 Implementing the approaches suggested in this paper will introduce new complications into the Bank's operations, it will somewhat increase administrative costs, and it will entail greater bank responsibility to private cofinanciers. We believe that the benefits to the developing countries will outweigh these costs, which are expected to be modest in any case. Both the quantity and quality of capital flows to the developing countries can be improved. This is crucial as we look to the great capital needs of developing countries and difficult capital markets expected in the 1980s.

Robert S. McNamara

Attachments

COFINANCING DEFINITIONS AND TERMINOLOGY 1/

1. As currently used in the Bank,2/ the term "cofinancing" refers in general to any arrangement under which funds from the Bank are associated with funds provided by other sources outside the borrowing country in the financing of a particular project. In some cases, funds from other sources may support parts of an entity's or agency's overall program in the sector to which the Bank project relates; such other financing is regarded as cofinancing if it is required to complete the financing plan for the Bank-supported project or if the Bank has played an active role in inducing the investment of funds by the other sources.

Types of Cofinancing

2. Joint Financing - the term "joint financing" refers to a cofinancing operation for which there is a common list of goods and services and where the financing of a disbursement for all or certain items is shared between the Bank and the colender in agreed proportions. Orders for all goods and services must be placed in accordance with procurement procedures acceptable to the Bank, normally the Bank's standard international competitive bidding rules.

3. Parallel Financing - the term "parallel financing" refers to a cofinancing operation in which the Bank and the colender finance different goods and services or parts of a project. Parallel financing is preferred by some colenders, either because they wish their financing to be identified with particular parts of a project for public relations purposes or because their procurement procedures are not compatible with the Bank's requirements for international competitive bidding. Under parallel financing arrangements, the Bank and the colender agree in advance on the parts of the project to be financed by each. The Bank then administers procurement related to its part of the project and the colender does likewise. Often, however, arrangements are made for regular exchange of information and joint supervision of the implementation of the project. Parallel financing permits greater flexibility in arranging for finance.

4. Participations - under some circumstances, the sale of participations in a Bank loan may be regarded as a type of cofinancing. This is particularly true where arrangements for the sale of participation are worked out prior to the making of the Bank loan in order to complete the required financing plan. In such cases, the Bank will administer the loan on behalf of the participant, who enters into a participation agreement with the Bank. Sales from the Bank's portfolio of portions of old loans, while releasing Bank funds for other purposes, are generally not regarded as cofinancing as the term is employed in the Bank.

1/ This Annex is derived from Operational Manual Statement 1.24.

2/ As used in this paper, "Bank" means Bank and IDA and "loan" means loan and credit.

Sources of Cofinancing

5. Official - official sources of cofinancing include governments, their agencies and multilateral financing institutions. This source is sometimes referred to as "donor" financing and the terms of such financing are often concessional in some degree.

6. Export Credits - as used generally in the Bank, export credits refer to financing which is linked to the procurement of certain goods or services from a particular country. The source of funds may be governmental or commercial or a mixture of both, and the actual financing may take the form of "buyer's credits" where loans are made by banks in the exporter's country directly to the importer (the borrower) or "suppliers' credits" where loans are made by the exporter to the importer in the recipient country. Export credits are often guaranteed or insured in a significant portion by an agency of the supplying country.

7. Private Institutions - financing by private institutions includes direct financing provided by commercial banks, insurance companies or other institutions or persons in the private capital markets outside the country of the borrower.

ATTACHMENT I

COFINANCING WITH WORLD BANK PROJECTS: FY73-79

	FY73		FY74		FY75		FY76		FY77		FY78		FY79	
	US$m	No. of Projects	US$m	No. of Projects	US$m	No. of Projects	US$m	No. of Projects	US$m	No. of Projects	US$m	No. of Projects	US$m	No. of Projects
Official Sources														
DAC - Bilateral	257.5	24	422.8	28	306.4	30	458.5	26	452.0	39	841.9	38	1,126.3	46
- Multilateral	28.6	2	9.4	2	25.1	2	106.5	3	-		1.2	1	257.2	27
OPEC - Bilateral	26.1	3	18.5	2	476.2	14	354.8	16	172.2	18	313.9	15	224.0	11
- Multilateral	-		-		41.5	3	171.9	14	232.1	16	139.1	15	59.1	10
Other	65.1	9	280.4	18	297.8	17	204.5	23	409.0	22	521.3	30	337.0	39
Total Official	377.3	38	731.1	50	1,147.0	66	1,296.2	82	1,265.3	85	1,817.4	99	2,003.6	133
Export Credits	71.1	3	514.2	10	711.4	7	663.6	10	333.3	10	375.0	11	651.5	15
Private Funds	-	-	60.0	1	76.3	2	286.0	5	423.7	10	219.2	11	549.8	16
Total Cofinancing	448.4	34	1,305.4	40	1,934.9	55	2,245.8	65	2,022.3	71	2,411.6	78	3,204.9	107
Of Which: Foreign Cost	407.7		1,290.8		1,876.6		2,157.7		1,917.5		2,187.5		2,625.8	
Local Cost	40.7		14.6		58.3		88.1		104.8		224.1		579.1	
Financing By World Bank	751.1		1,268.2		1,349.4		1,871.6		2,199.7		2,446.0		4,085.0	
Of Which: IBRD	445.9		1,102.6		1,018.3		1,485.6		1,805.2		1,811.7		2,952.8	
IDA	305.2		165.6		331.1		386.0		394.5		634.3		1,132.2	
Total Project Cost	2,783.2		5,197.4		8,746.2		8,927.2		8,333.4		11,242.3		13,633.6	
Percentage Shares														
Official Sources	84.1		56.0		59.3		57.7		62.7		75.4		62.5	
Export Credits	15.9		39.4		36.8		29.5		16.5		15.5		20.3	
Private Funds	-		4.6		3.9		12.7		21.0		9.1		17.2	

Note: Breakdown of the number of cofinanced projects by source may exceed total, as several Agencies participate in cofinancing a given project.

Source: Senior Adviser Cofinancing/PAB.

ATTACHMENT 2

COLENDER TERMS FY79

Country	Board Approval Date	Export Credits Amount ($m)	Export Credits Mat. --(Yrs.)--	Export Credits Grace --(Yrs.)--	Export Credits Interest (%)	Private Amount ($m)	Private Mat. --(Yrs.)--	Private Grace --(Yrs.)--	Private Interest L=LIBOR
Portugal	1/ 4/79	31.0	-	-	-	28.8	10	4	L+7/8
Romania	11/28/78	12.9	8	2.5	7.5	-	-	-	-
	1/ 9/79	11.0	8	3	10.0	-	-	-	-
	3/20/79	-		-	-	100.0	10	4	L+5/8 $70m. L+3/4 $30m.
Yugoslavia	3/10/78	-	-	-	-	20.0	12	5	L+7/8
Brazil	3/ 6/79	-	-	-	-	90.0	10	4	L+1-1/2
	6/ 7/79	-	-	-	-	60.0	10	5	12
Colombia	11/14/78	-	-	-	-	22.9	10	5	L+3/4 L+7/8 after 3 yrs.
	6/12/79	30.1	12	4	8.5	-	-	-	-
Dominican Republic	5/17/79	-	-	-	-	10.0	10	4	L+1-1/4 L+1-3/8 after 4 yrs.
Paraguay	6/21/79	-	-	-	-	7.0	12	6	L+7/8 L+1 after 6 yrs.
Uruguay	4/17/79	-	-	-	-	5.0	10	3.5	L+7/8

C

International Bank for Reconstruction and Development

FOR OFFICIAL USE ONLY

SecM80-128

FROM: Vice President and Secretary

February 22, 1980

BRANDT COMMISSION PROPOSALS

2/22

Attached is a memorandum entitled "Brandt Commission Proposals" dated February 21, 1980 from the President.

Distribution:

Executive Directors and Alternates
President
Senior Vice President
President's Council
Vice Presidents, IFC
Directors and Department Heads, Bank and IFC

FOR OFFICIAL USE ONLY

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

Office of the President

February 21, 1980

MEMORANDUM TO THE EXECUTIVE DIRECTORS

SUBJECT: BRANDT COMMISSION PROPOSALS

In the Board meeting on February 12, 1980, Tuesday, I indicated that we intend to prepare a series of papers on the recommendations of the Brandt Commission which relate to the World Bank. Attached is a list of such proposals. We have also indicated a tentative schedule for submitting the papers to the Board for their consideration, assuming the Board wishes to discuss them.

Robert S. McNamara

BRANDT COMMISSION PROPOSALS RELATING TO THE WORLD BANK

Proposal	Tentative Date of Submission to Board
1. Expand Program Lending by the Bank. (p. 291) /a	Board Memo R80-17 (IDA/R80-22) of 2/5.
2. Provide for greater co-financing by the Bank. (pp. 256, 278)	Board Memo R80-22 (IDA/R80-28) of 2/19.
3. Abstain from imposition of political conditions on operations of IFIs. (p. 291)	5/27
4. Plan to effectively utilize the increased borrowing capacity of the Bank resulting from the doubling of its capital. (p. 291)	6/15
5. Change the Bank's present "gearing ratio" /b so as to raise its lending capacity. (p. 291)	7/8
6. Develop an action program to reduce absolute poverty in the poverty belts of Africa and Asia during the 1980s. (p. 282)	7/8
7. Analyze the likely debt and debt servicing problems in various categories of LDCs and the capacity of existing private and public institutions to meet these needs. (p. 292)	7/15
8. Define the role of the surplus countries in financing the adjustment problem of developing countries (p. 239)	7/22
9. Substantially increase Bank financing for exploration and development of energy resources. (p. 292)	7/22

/a References are to page numbers of the Brandt Commission Report.

/b The ratio of receivables to capital, as prescribed by the Articles of Agreement.

Proposal	Tentative Date of Submission to Board
10. Use the Bank's guarantee to improve access of developing countries to capital markets. (p. 292)	8/5
11. Develop an action program to increase food output in low-income, food-importing developing countries during the 1980s. (p. 280)	8/12
12. Provide greater participation of LDC staff in Bank management. (p. 275)	8/12
13. Set up a new facility for financing the development of minerals and energy (p. 292)	9/9
14. Provide greater decentralization of the management of the Bank's operations. (p. 275)	9/9
15. Provide borrowing countries a greater role in the decision-making process in the Bank. (p. 275)	9/23
16. Examine the possibility of the Bank's refinancing export credits for capital goods. (pp. 234-235)	11/11
17. Consider the creation of a new international financial institution - a World Development Fund - to supplement existing institutions and to diversify lending policies and practices.	1/14/81

2/21/80

D

Record Removal Notice

File Title	Barcode No.
Board Actions - Brandt Commission - Board papers 01	1770707

Document Date	Document Type
Mar 21, 1980	Board Record

Correspondents / Participants

Subject / Title
Lending for Structural Adjustment - Statement by Mr. Stern

Exception No(s).

☐ 1 ☐ 2 ☐ 3 ☐ 4 ☐ 5 ☐ 6 ☐ 7 ☐ 8 ☐ 9 ☐ 10 A-C ☐ 10 D ☐ Prerogative to Restrict

Reason for Removal
Board Record

Additional Comments
Declassification review of this record can be initiated upon request

The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information. This Policy can be found on the World Bank Access to Information website.

Withdrawn by	Date
Chandra Kumar	Aug 4, 2014

E

Record Removal Notice

The World Bank Group Archives & Records Management

File Title	Barcode No.
Board Actions - Brandt Commission - Board papers 01	1770707

Document Date	Document Type
Mar 31, 1980	Board Record

Correspondents / Participants

Subject / Title
Lending for Structural Adjustment

Exception No(s).

☐ 1 ☐ 2 ☐ 3 ☐ 4 ☐ 5 ☐ 6 ☐ 7 ☐ 8 ☐ 9 ☐ 10 A-C ☐ 10 D ☐ Prerogative to Restrict

Reason for Removal
Board Record

Additional Comments
Declassification review of this record can be initiated upon request

The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information. This Policy can be found on the World Bank Access to Information website.

Withdrawn by	Date
Chandra Kumar	Aug 4, 2014

F

FOR EXECUTIVE DIRECTORS' MEETING

For consideration on July 10, 1980

R80-145

May 30, 1980

FROM: Vice President and Secretary

BRANDT COMMISSION RECOMMENDATION NO. 3 CONCERNING IMPOSITION OF POLITICAL CONDITIONS ON OPERATIONS OF MULTILATERAL FINANCIAL INSTITUTIONS

As referred in the President's memorandum of February 22, 1980 (SecM80-128), attached hereto is a memorandum dealing with the Brandt Commission Recommendation No. 3 concerning imposition of political conditions on operations of multilateral financial institutions.

Questions on this document may be referred to Mr. Benjenk (extension 72466).

Distribution:

Executive Directors and Alternates
President
Senior Vice President
President's Council
Vice Presidents, IFC
Directors and Department Heads, Bank and IFC

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

DECLASSIFIED **FOR OFFICIAL USE ONLY**

AUG 04 2014

WBG ARCHIVES

Office of the President

May 30, 1980

MEMORANDUM TO THE EXECUTIVE DIRECTORS

Subject: Brandt Commission Recommendation No. 3 Concerning Imposition of Political Conditions on Operations of Multilateral Financial Institutions 1/

Recommendation: "Lending through international financial institutions should be improved through: ... 3. Abstaining from the imposition of political conditions on the operations of multilateral financial institutions." 2/

1. The recommendation appears in the chapter of the Brandt Commission Report entitled "A New Approach to Development Finance", which puts forward a number of proposals for a substantial increase in the transfer of resources to the developing countries. International financial institutions (IFIs) are called upon to play an expanded role in resource transfers.

2. The recommendation is addressed implicitly to governments in their sovereign capacity, not to IFIs in general or to the Bank specifically. Assuming that the recommendation is found to have merit, implementation is not fully within the authority or competence of the Governors in their representative capacity, of the Executive Directors, of the Bank as an institution, or of its management, as would be possible with respect to the recommendations concerning, for example, use of the Bank's guarantee powers, financing for development of energy resources or program lending. But because the recommendation has significant implications for the Bank, and indeed has as an explicit objective the improvement of lending through IFIs, it has been included in the list of proposals to be presented for Board consideration.

3. The Report does not define "political conditions", nor does it give examples of what the Commission had in mind. But in its application to the Bank the recommendation clearly recognizes that the Bank cannot perform effectively as an international development institution if its operations are constrained by other than economic considerations. That the Bank's founders conceived of the Bank as a "non-political" organization, and sought to ensure that character, is evident from its Articles. They enjoin member governments from attempting to weaken the international character of the duties of the President, officers and staff; they enjoin the Bank and its officers from interfering in a member's domestic political affairs, and from taking account of its political complexion in making their decisions, which are to be based

1/ The reference is to the order of recommendations listed in SecM80-128, dated February 22, 1980.

2/ Brandt Commission Report, p. 291.

on economic considerations alone.[1/] Similarly, the "relationship agreement" between the Bank and the United Nations, approved by the Bank's Board of Governors and by the General Assembly of the United Nations in 1947, recognizes that

> "By reason of the nature of its international responsibilities and the terms of its Articles of Agreement, the Bank is, and is required to function as, an <u>independent</u> international organization." 2/ (Underscoring added.)

In addition, the United Nations recognizes that "the action to be taken by the Bank on any loan is a matter to be determined by the independent exercise of the Bank's own judgment" in accordance with its Articles, and that it would be "sound policy to refrain from making recommendations to the Bank with respect to particular loans or with respect to terms or conditions of financing by the Bank." While the recommendations which the United Nations undertakes to refrain from making are not explicitly characterized as "political", the implication that this was the intention is reinforced by the further provision under which the Bank, for its part, recognizes that the United Nations and its organs "may appropriately make recommendations with respect to the <u>technical aspects of</u>...plans, programmes or projects." 3/ (Underscoring added.)

1/ Article III, Section 5(b): "The Bank shall make arrangements to ensure that the proceeds of any loan are used only for the purposes for which the loan was granted, with due attention to considerations of economy and efficiency and without regard to political or other non-economic influences or considerations."

Article IV, Section 10: "The Bank and its officers shall not interfere in the political affairs of any member; nor shall they be influenced in their decisions by the political character of the member or members concerned. Only economic considerations shall be relevant to their decisions, and these considerations shall be weighed impartially in order to achieve the purposes stated in Article I."

Article V, Section 5(c): "The President, officers and staff of the Bank, in the discharge of their offices, owe their duty entirely to the Bank and to no other authority. Each member of the Bank shall respect the international character of this duty and shall refrain from all attempts to influence any of them in the discharge of their duties."

2/ Article I, Section 2 of the relationship agreement. The text of the agreement appears in the Basic Documents Manual.

3/ Article IV, Section 3. The relationship agreement does provide that in the conduct of its activities the Bank will have "due regard" for decisions of the Security Council under certain provisions of the U.N. Charter.

4. Maintenance of the non-political character of the Bank and the prescription of its Articles that only economic considerations shall be relevant to decisions of the Bank (including the Executive Directors) 1/ and its officers do not preclude those decisions or the Bank's loan covenants from taking account of the political situation in the borrowing country to the extent that it affects the economic justification for a proposed loan or the successful implementation of the project to be financed. The Bank's appraisal of that situation has sometimes been a critical element in judgments of country creditworthiness or in the determination of the conditions of a loan.

5. It is not to be expected that attitudes of individual governments in respect of Bank policy and operations will be wholly uninfluenced by political considerations. The plea of the Brandt Commission was addressed to situations in which the political element is predominant: for example, efforts by a member to make the Bank an extension or instrument of its own political or protectionist interests.

6. The Bank has had experience of such attempts, notably by proposals to restrict the use of Bank funds. While other illustrations could be elaborated (for example, attempts to limit application of procurement guidelines, or to condition IDA contributions or entry into a country's capital market on representation of the country at the managerial level), experience in three areas in particular appears to account for the Commission's concern: conditions on lending to countries regarded as violators of human rights, on lending to particular countries, and on lending for production of a particular commodity.

Human Rights

7. Some members have opposed financial or technical assistance by IFIs to countries in respect of which serious questions of human rights violations have been raised, unless the assistance is directed toward meeting the basic human needs of the people of those countries or would directly benefit the poorest of the population. But most members, citing the Articles, have expressed the view that the application of such non-economic criteria in evaluating loans would be beyond the competence of the institution. There have been some exceptional instances in which the Bank has found that a country's actions and attitudes in respect of human rights have had an adverse effect on its economic situation. In those instances, application

---

1/ In 1977, the Bank's Legal Department interpreted the reference to "the Bank" in Article IV, Section 10 as including "all the Bank organs and persons responsible for the conduct of its operations", concluding that the Executive Directors, who are responsible under Article V, Section 4(a) for the conduct of the general operations of the Bank, are "as bound by the provisions of Article IV, Section 10 as 'the management' and officers of the Bank."

of the Bank's economic criteria has precluded presentation of loans and credits to the Board, on the ground that, as long as the particular circumstances prevailed, loan or credit proceeds could not be effectively employed for economic development. When the economic situation has again permitted effective use of funds provided, lending has been resumed.

Commodity Lending

8. Proposed legislation would have precluded use of a member's contributions to IFIs to establish or expand production in developing countries of certain commodities. The President and the General Counsel of the Bank expressed the view that the Bank/IDA could not accept funds with such conditions attached. The same conclusion was reached for the Inter-American Development Bank by its General Counsel.

9. Legislation requires a member to oppose IFI support for the production for export of any commodity which is in surplus on world markets where that support could adversely affect the country's producers of that or a competing commodity. Bank policy with respect to commodities which are in surplus is normally to limit financing of new production to countries with a high degree of comparative advantage in the production of the commodity concerned or with few export alternatives, or to projects for rehabilitation and rationalization involving no increase in output. Before developing a project for export production, the Bank takes account of the effect on the world market which increased production can be expected to have. But if the Bank's objective analysis leads it to conclude that, on economic criteria, a loan is justified, it has been put to the Board.

Lending to Particular Countries

10. Proposals under consideration would have precluded IFIs' use of a member's contributions for lending to named individual countries. As stated in paragraph 8, the Bank's General Counsel advised that, under their respective Articles, neither the Bank nor IDA could accept funds with conditions attached. The opinion cited not only Article IV, Section 10, but also Article VII, Section 6, which provides that

> "To the extent necessary to carry out the operations provided for in this Agreement and subject to the provisions of this Agreement, all property and assets of the Bank shall be free from restrictions, regulations, controls and moratoria of any nature."

Similar conclusions were reached, under the Articles of their institutions, by the counsel of the Inter-American Development Bank and the Asian Development Bank.

11. Other examples may be cited:

a. Legislation has required opposition to lending to any country which developed a nuclear explosive device unless it was or became a party to the treaty on non-proliferation of nuclear weapons.

b. For many years, a number of the Bank's members opposed every proposed loan to a particular member country, and recently one member has consistently opposed lending to another member.

c. The existence of a territorial dispute between two member countries was the reason for the opposition of six other member countries to lending to one of the parties to the dispute.

12. There have also been collective efforts, by the United Nations, to impose restrictions on Bank lending. In 1965, a committee of the U.N. General Assembly and later the Assembly itself called upon the members of the United Nations, all the specialized agencies "and in particular" the Bank and the International Monetary Fund to refrain from extending financial, economic or technical assistance to one country in Europe and one in Africa as long as these countries followed their colonial or apartheid policies. A similar resolution was adopted in 1966.

13. In providing the Executive Directors with the text of these resolutions in 1966, the President of the Bank told the Directors that, in view of the provisions of Article IV, he proposed to continue to treat requests for financing from the two countries in the same manner as applications from other members. He noted, however, that the "situation in Africa could affect the economic development, foreign trade and finances" of the two countries and that it would therefore "be necessary, in reviewing the economic conditions and prospects of these countries, to take account of the situation as it develops." Loans were made to each of the countries in 1966. The Bank's General Counsel explained the Bank's position to the General Assembly committee, and exchanged written opinions with the U.N. Legal Counsel. The latter acknowledged the relevance of Article IV, Section 10 of the Bank's Articles but argued that it was intended to preclude interference in the internal political affairs of members. In the opinion of the Bank's General Counsel, however, there was no justification for adding the qualification "internal", and the Articles precluded the Bank from interfering or attempting to interfere with a member's relations with other states. The opinion added that "the Bank may and does take into consideration, and is influenced in its lending decisions by, the economic effects which stem from the political character of a member and from the censures and condemnations of that member by United Nations organs. ... What it is precluded from considering is the political character of a member

as an independent criterion for decision." The General Counsel added that in his view the provision of Article IV, Section 10 "is no more than a reflection of the technical and functional character of the Bank" and that "the characterization of the Bank as a financial and economic agency and not a political one was explicitly recognized by the United Nations" in the relationship agreement. The position of the Bank's General Counsel was endorsed (with some dissents) by the Executive Directors. Each side maintaining its position, the President of the Bank and the Secretary-General of the United Nations in an exchange of letters in August 1967 agreed to let the matter rest. 1/

Conclusion

14. While attempts have been made from time to time to introduce non-economic considerations, reflecting national political concerns, into the Bank's decision-making, the majority of the membership has resisted these attempts. Consistent with the prescriptions of the Bank's Articles, they have effectively maintained the Bank's character as a functional, non-political, international development organization.

15. Given the present and foreseeable overwhelming requirements of the developing countries for development assistance, it is more important than ever to preserve the strength and reputation of the Bank as an effective instrument for raising funds and channeling them to the developing countries. The Bank cannot and does not ignore the political realities of the world within which it operates. But it is in the interests of all of its members to assure that its operations continue to be insulated, as the drafters of its Articles intended, from the impact of national political attitudes which necessarily reflect changing national concerns. To be responsive to such considerations would be incompatible with the long view which the Bank as a development institution must take.

1/ No loans were in fact made to one of the countries subsequent to the one mentioned in the text until 1976, when lending was resumed. No loan has been made to the other country since 1966. U.N. resolutions nevertheless continue to call upon the Bank to cease its assistance to that country.

16. Thus far, attempts to impose political conditions on the Bank's operations have been limited. But the Brandt Commission has perceived a trend and in that trend a threat to the Bank's ability to perform the function for which it was established. There is a danger that its ability to attract capital on the scale required from governments and the private market, to carry out an effective lending program, and in other respects to discharge its responsibilities to further the economic development of its members may be adversely affected. It is for that reason that the Commission's recommendation against the imposition of political conditions on the operations of the IFIs should be supported.

Robert S. McNamara