



DEVELOPMENT COMMITTEE
(Joint Ministerial Committee
of the
Boards of Governors of the Bank and the Fund
On the
Transfer of Real Resources to Developing Countries)



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NOTE FROM THE PRESIDENT OF THE WORLD BANK

Attached is a Note from the President of the World Bank, James D. Wolfensohn, for the seventy-first meeting of the Development Committee, to be held on Sunday, April 17, 2005, in Washington, D.C.

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PRESIDENT'S NOTE TO THE DEVELOPMENT COMMITTEE

I. INTRODUCTION

1. 2005 is a milestone year for the international development agenda. It marks a third of the way to the target year of 2015 for achieving the Millennium Development Goals (MDGs); world leaders will meet in September to evaluate progress on what has been achieved and what needs to be done if we are to meet the MDGS. The Development Committee is the first of a series of discussions we will be having on the development agenda in 2005, including the meeting of the Council of European Ministers later this month, the High Level Dialogue on Financing for Development and the ECOSOC meetings in June, the G8 Summit at Gleneagles in July, the High Level Plenary Meeting in September, and the WTO Ministerial Meeting in Hong Kong in December. Not all of the issues to be addressed can be resolved at the Spring Meetings here, but this Development Committee meeting provides an important opportunity to shape and give impetus to the 2005 agenda and secure political commitment for achieving results.

2. As you all know, for some time I have been saying that there is little disagreement on what needs to be done by the developing countries themselves, by their developed country partners, and by the multilateral institutions. The goals have been set at the Millennium Summit in 2000 and the elements of the bargain spelt out in Monterrey, Johannesburg and in Doha. Yet three years after Monterrey there is a sense that different parties are still waiting for others to make a move. We are now better positioned than ever before in the fight to eradicate poverty. If we fail to take the opportunity, the risks are great not only of not meeting the MDGs, but of failing to achieve the ultimate goal we all seek: the goal of a peaceful, prosperous and secure planet. 2005 is thus a year of great opportunity and also a year of grave risk.

3. We will have the opportunity to discuss all aspects of what needs to be done at our meeting on April 17. The annual *Global Monitoring Report* (GMR) – which the Committee first asked for three years ago, after Monterrey – sets out clearly what progress has been made, and what remains to be done. Along with the GMR, we have also prepared separate progress reports for the Committee on *Financing the Development Agenda*, and *Voice and Participation of Developing and Transition Countries in Decision making at the World Bank and the International Monetary Fund*. I look forward to our discussions and your guidance on all these issues.

4. There are additional risks to progress in the period immediately ahead from developments in the global economy. Over the last few years, developing countries in general have experienced a period of exceptional growth: 6.6 percent last year, compared with growth of 3.2 in high-income countries. This reflects very strong growth among some of the developing world's largest countries (China, India and Russia grew 9.5, 6.8 and 7.1 percent respectively). Other developing countries in East Asia and Pacific, South Asia, and Europe and Central Asia also recorded strong growth; and in the Middle East

and North Africa, Latin America and the Caribbean, where the pace of expansion was less, it was nevertheless much stronger than in the recent past. Even in Sub-Saharan Africa, where the pace of the expansion was lower, it was nevertheless much stronger than in the recent past. Following substantial structural and macroeconomic reforms during the 1980s and 1990s, trend growth rates in all developing regions have been rising.

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

6. In keeping with past practice, in this note I am also reporting on progress and actions on some of the other issues the Committee has considered in the past. We will have opportunities to discuss some of these issues informally at the Committee's lunch.

7. As this will be the last meeting of the Committee that I will attend as President of the World Bank, I would also like to take this opportunity to express my deep appreciation and thanks for the support and wise guidance that past and present members of the Committee have given over the last 10 years. It is one of the abiding strengths of this extraordinary institution that Paul Wolfowitz who will succeed me as President will be able to benefit from the same support and guidance in the future.

II. ASSESSING PROGRESS ON THE DEVELOPMENT AGENDA

8. In September, world leaders will meet in New York to review progress on the commitments they made in the Millennium Declaration adopted at the UN Millennium Summit in 2000. 2005 offers perhaps a last opportunity to make adjustments, and further commitments needed if the MDGs are to be met. The Secretary General has in his own recent review of the Millennium Declaration given a compelling assessment of progress and what remains to be done. The recent report of the Commission for Africa, chaired by Prime Minister Tony Blair, gives a detailed assessment of progress and challenges in Africa – the continent most at risk of falling seriously short of meeting any of the MDGs. This meeting of the Development Committee is therefore a key stepping stone to the September Summit. The GMR, prepared by staffs of the Bank and the Fund with major inputs from the UN, WTO and other multilateral agencies, gives a sobering assessment of progress in implementing actions and policies needed to achieve the MDGs, and what

further action is now needed. I believe it provides an excellent basis for the Committee's discussion.

9. The framework underpinning the GMR is the Monterrey Consensus framework that describes the roles and responsibilities of developing countries, their developed country partners, and the multilateral institutions in achieving the MDGs. The GMR provides an assessment of performance and prospects against that framework and identifies an action plan to make the progress needed to achieve our goals. This year's GMR confirms the assessment in the first report that we reviewed at the Development Committee meeting last spring: that most MDGs will not be met in most countries on present trends. While prospects are promising for meeting the income poverty goal at a global level, with particularly rapid progress in China and India and steady improvements in most other regions, the incidence of poverty in Sub-Saharan Africa rose between 1990 and 2001, and most countries in the region are likely to fall far short of the poverty goal. Indeed, Sub-Saharan Africa as a region is not on-track to achieve any of the MDGs by 2015 and is the only region where child malnutrition is increasing.

10. The risks of falling short are much more pervasive across regions with respect to the other MDGs. The world has already missed its first MDG target set for 2005: the achievement of gender equality in primary and secondary education. Most regions are falling short, some seriously, of the health related goals – reduction of child and maternal mortality, expansion of access to basic sanitation – and the number of people with HIV/AIDS continues to grow. In education, the pace of progress is too slow to ensure attainment of the universal primary completion goal in three of the six developing regions (i.e., South Asia, the Middle East and North Africa, and Sub Saharan Africa).

11. Looking ahead, and with just a decade to go to 2015, achieving all the MDGs presents an enormous challenge. But we know that with the right policies and actions rapid progress is possible, and the success of the better performing regions and countries, including in Sub Saharan Africa, provides hope for others. So while it important to check that we do indeed have a common perception about progress so far, I hope we can focus our discussion on the key areas where we need to take action. I mean concrete decisions and actions that all of us – developing countries, industrial countries, and multilateral institutions acting together as a global community – agree on and begin to implement this year.

12. The GMR provides a good, if sobering, assessment here as well – of what we are doing well, and what more we need to do to get back on track to meeting the MDGs. It highlights the following five points.

- *Country Strategies.* Many of the poorest countries need to strengthen country-owned and -led poverty reduction strategies (PRSs), with better links with medium-term budgetary frameworks; more ambitious PRSs should provide the anchor for country actions to achieve the MDGs, and donors should act faster to align and harmonize their assistance around these strategies.
- *Investment Climate.* Many developing countries need to do much more to improve the environment for strong, private sector-led economic growth. Of

particular importance in this regard are efforts to build deep, efficient and inclusive financial systems, strengthen fiscal management, with a focus on the structure of public spending; improve the enabling climate for private activity, by removing unnecessary regulatory and institutional constraints and strengthening economic infrastructure; and strengthen the quality of governance – upgrade public sector management and combat corruption.

- *Service Delivery.* We all need to do more to significantly scale up the delivery of human development services through a rapid increase in the supply of skilled service providers (health workers, teachers); increased and more flexible financing for these recurrent cost-intensive services; and improved governance along the service delivery chain to ensure that money produces results.
- *Trade.* We need bold actions to dismantle the barriers to trade to achieve an ambitious outcome of the Doha Round, which fully realizes its development promise, completing the Round no later than 2006, and by stepped-up assistance to poor countries to address behind-the-border constraints to their trade capacity, through investments in critical trade-related infrastructure.
- *Financing development.* Finally, the level and effectiveness of official development assistance needs to be increased significantly. In line with rising absorptive capacity, the GMR suggests that ODA should be doubled from current levels, particularly to low-income countries and Sub-Saharan Africa, and that proposals for additional HIPC debt relief should be brought to closure in 2005—and without cutting into new ODA commitments.

III. A PROGRAM OF ACTION

13. 2005 is a year for meeting key challenges. Our successors may look back and see 2005 as the year when decisions were made and commitments met that resulted in a more prosperous and secure world. Or they may look back and see it as a year of missed opportunity. There is no doubt in my mind that we would all prefer the former as our legacy. The question is whether we and the governments and institutions we represent are ready to act to achieve it. Let me spell out in more detail the concrete actions that I see as needed, starting this year, if we are to succeed, including actions that the Bank must take to support the process.

A country by country approach

14. **First**, we all have to have to scale up our efforts on the ground, country by country.

15. In *low-income countries* (LICs) we have a sound basis for doing this, accepted by all partners, in the Poverty Reduction Strategy (PRS) approach. Forty-seven countries are now implementing PRSs as country-led frameworks for development and achieving the MDGs, providing an anchor for both domestic efforts and external support. But in most countries the process needs to be deepened further, in particular by strengthening the link with medium-term expenditure frameworks and annual budgets, increasing transparency and better articulation of agendas for spurring economic growth. In many countries there

is scope for using PRSs to assess options for accelerating policy reform matched by extra external assistance. In all countries, those providing assistance can and should do more to align and harmonize their assistance with country policies and systems. In the Bank we are continuing to support this approach, and to adapt our own procedures and instruments accordingly. We are currently undertaking jointly with the Fund a review of five years of implementation experience, seeking to draw lessons and identify good practices; to identify recommendations for strengthening implementation; and to clarify an appropriate framework for monitoring results. We are also currently completing a review of experience with our core instrument for supporting PRSs, the Poverty Reduction Support Credit (PRSC). However, I believe that the level of ambition relative to PRSs can and must be raised: ambition on country actions to meet the MDGs, ambition on addressing capacity constraints and ambition on the volume and quality of financing needed to support country efforts.

16. We are also working with other development partners to improve the way we provide support to low-income fragile states, the so-called *low-income countries under stress* (LICUS). Effective international engagement with fragile states is essential for global security, for the well-being of the 500 million poor people living in these countries and for development in neighboring countries. There is increasing recognition by all that initial stabilization and peace-keeping efforts in the most fragile states need to be strengthened by building state capacity, state legitimacy, and viable economic recovery if these countries are not to slip back into conflict. Security and development linkages are very important in these countries. The Bank has collaborated with the UN Development Group to produce a new planning tool integrating political, security, economic and social issues in one unified results framework. In January, the Bank co-sponsored a *Senior Level Forum on Development Effectiveness in Fragile States* in London which helped develop a set of *Principles for Good International Engagement* in fragile states. We will also continue with our own internal reforms to strengthen and better support Bank country teams working in these countries, and to position ourselves better to move quickly when an opportunity for transition occurs, as it has in Haiti, Liberia and Sudan. The LICUS Implementation Trust Fund has helped fill a critical financing gap for countries in non-accrual with the Bank. The framework for IDA 14 includes a provision for exceptional assistance to failed states which do not fully meet the post-conflict criteria, as was the case with Haiti.

17. Successful and sustained development in *middle-income countries* (MICs) will also be crucial to meeting our global development goals. This highly diverse group of countries is home to almost 70 percent of the world's poor, and some of these countries play key roles as regional anchor economies. As a group, their performance is critical to delivery of many global public goods, ranging from global environmental sustainability to global financial stability. They are the client base of the IBRD and regional development banks for non-concessional lending. In the Bank, we are successfully implementing the Management Action Plan for Enhancing Bank Support to MICs that we launched a year ago to increase our responsiveness to clients' demand for high quality lending, risk management products, and knowledge services. It will be important globally, for all development partners including MDBs, to find ways to work more

closely together and with MICs themselves to enhance the effectiveness of our joint efforts to support their development. We have to recognize that different parties have different objectives in providing support, and that the diversity of MICs means that approaches will differ greatly in different countries. But the potential gains from stronger cooperation are great, and over the months ahead we will be continuing a series of discussions with donors, other MDBs and the MICs to identify ways to enhance cooperation, including greater use of techniques that combine the instruments and aid modalities offered by different parties. As the separate paper on *Financing the Development Agenda* points out, greater use of a variety of techniques for blending donor grant support with MDB lending could be a way to greatly enhance the total flow of resources to support of MDG related investments in MICs.

18. We are also looking at the way the Bank supports policy reform in all three groups of countries in our current *review of practice in the use of conditionality*. This review – requested by the Committee at its last meeting – builds on previous reviews of policy-based lending, including the focus and effectiveness of conditionality, which eventually led to an update of the Bank’s policy in September 2004, when Development Policy Lending replaced adjustment lending. Through consultations and surveys we are seeking to reflect not only the Bank’s own experience but also the views and experience of borrowing countries, bilateral partners and civil society organizations (CSOs). The conclusions of the review will be presented at the Annual Meetings. Although conditionality has been a controversial topic for many years, I believe that we are reaching a point where it may be becoming something of a misnomer. What we are now implementing in most countries is a partnership with a mutual commitment to support medium-term policy and institutional changes, in which the country decides and implements its own reform agenda, as in PRSs; the Bank and IDA, and in many cases other donors also, advise on and support good policy reform agendas – with associated frameworks for measuring results – as appropriate with policy based loans and grants. These must be based on a few critical measures that embody real ownership and that will produce better results, rather than on an exhaustive list of conditions.

Country actions to improve the environment for stronger growth

19. **Second**, progress at the country level – in both low- and middle-income countries - hinges above all on policy decisions and actions taken by countries themselves, critically the implementation of policies that provide a supporting environment for faster, private sector led growth. Achieving faster economic growth must be at the center of the strategy. To meet the MDGs, Africa needs to double its growth rate.

20. I have been saying this for years: nothing will work unless countries strengthen governance and tackle the cancer of corruption. The Commission for Africa report gives the same message, correctly drawing attention to actions that advanced countries can also take to help the process. All Bank country assistance strategies (CASs) now address governance issues, with lending volumes linked to progress in governance and anti-corruption. In some of the higher risk countries, governance and anti-corruption have become the anchors for the entire country program. Some 20 percent of our lending

commitments are now for good governance, public sector reform, and rule of law. We have also developed governance indicators and other diagnostic tools which are being increasingly used by other development partners such as the Millennium Challenge Account (MCA) of the United States as guides for their operations. And we have also addressed issues of corruption at home: so far, more than 300 companies and individuals have been sanctioned from doing business with the Bank, and their names and sanctions posted on the Bank's external website. It will be important for advanced country governments to do all they can to assist by tackling potential sources of corruption in their own countries and increasing transparency. The World Bank Group has continued to strongly support the Extractive Industries Transparency Initiative (EITI) by providing on-the-ground support to governments who have embraced the initiative and wish to move to make their extractive industry revenues transparent.

21. Developing country governments need to take further actions on two fronts to create an enabling climate for private activity, which is key to accelerating growth and poverty reduction.

- First they need to act to remove unnecessary regulatory and institutional constraints, simplifying regulations on starting a business, securing property rights and strengthening contract enforcement and the rule of law. Access to finance also needs to be improved. Countries can and should use improved diagnostics and metrics of the private business environment that the Bank has helped develop – the *Doing Business* indicators, country investment climate surveys – to guide action and monitor progress. Similarly, countries should build on the findings of the FSAP and ROSC programs – to improve their financial sector infrastructure and regulatory capacity. The Bank is also beginning to support such actions with lending operations. In addition, the Bank Group is committed to building inclusive financial systems that work for all members of society and has committed \$1.35 billion in support of micro-, small and medium enterprises (MSMEs) so far in FY05.
- Second, countries should substantially increase investment in the physical infrastructure needed to support private activity, recognizing that the bulk of the increase in infrastructure investment, particularly in Sub-Saharan Africa, will need to come from the public sector.

22. Macro economic policies that deliver stability and growth are also central. Particularly in poor countries, it is clear there is much to be done to deepen macroeconomic management, with a focus on fiscal management, the structure and planning of public spending, and ensuring debt sustainability. In this context a move towards more grant finance is welcome, so long as the present-value of future aid flows is not negatively affected. So too is the recognition of the interrelationship between fiscal policy and long-run growth. While fiscal policy has legitimately been viewed as a tool for short-run economic stabilization, recent policy debates (including the discussion of "fiscal space") have asked whether its effect on long-run growth should not be re-emphasized. This comes at a time when private flows have receded and the links between

infrastructure investments, competitiveness, and growth are seen as being important aspects of the poverty reduction challenge. In this context, the Bank will renew its work on fiscal composition and help countries in examining their infrastructure needs in the context of viable and financable development strategies.

Improving delivery of human development services

23. **Third**, we need to help countries act to achieve a major scaling up in delivery of education and health services, areas where there is greatest danger of failing to meet the MDGs in most countries. Primary education, basic health care and control of diseases such as HIV/AIDS, women's access to education and health care, and water and sanitation infrastructure closely linked to health outcomes, are all priorities. The shortfalls are most serious in Sub-Saharan Africa. Critical elements in scaling up include increasing the supply of skilled service providers, mobilizing flexible and predictable financing and improving management of the service delivery chain to ensure that money produces results.

24. In accelerating progress in meeting the *health-related MDGs*, new partnerships and global initiatives that have emerged in the past five years are providing a new impetus and a fresh flow of funds for specific public health issues. But not being integrated into national policies and institutions, their effectiveness is limited and could threaten their sustainability. Too much donor assistance flows outside the normal country budget processes, creating transactions costs for countries and often undermining country ownership. The third High Level Forum on health-related MDGs, to be held in November in Paris, will discuss these issues and seek to build consensus on actions to address them. HIV/AIDS poses a special threat: with 40 million people now infected with HIV, over 20 million already dead, and more than 15 million AIDS orphans world-wide, HIV-AIDS is destroying the development effort of decades in many countries, especially in Africa. The international community has substantially increased its commitments to fighting the epidemic – from about \$300 million annually ten years ago to \$4-5 billion last year. While more resources are needed, especially for treatment, the most immediate challenge is implementation: ensuring that existing commitments are used quickly, efficiently and effectively. We are seeking to define the Bank's contribution to this global effort in a new World Bank HIV-AIDS Action Program, building on our areas of comparative advantage such as strengthening HIV advocacy and program planning at country level; providing strategic funding to increase impact and fill gaps; enhancing country implementation systems, and collecting and disseminating knowledge to improve performance.

25. In *education* the Education for All (EFA) Fast Track Initiative (FTI), launched in 2002, has emerged as the key instrument for donor harmonization and support to countries in meeting the education MDGs. The FTI embodies the Monterrey Consensus, with both country and donor performance monitored against agreed indicators. Challenges remain, however, both to ensure sustainable financing for the 13 FTI-endorsed country programs (Ethiopia has been recently added), and to meet financing needs of 25 additional countries with sector programs which may be endorsed in 2005. The latter alone will require a \$2 billion increase in ODA. Despite overwhelming

evidence that teaching children how to read, write, and count can break the cycle of poverty that haunts the lives of too many of the world's children, boost economic growth and blunt the spread of AIDS, the financial support needed for the FTI is still lacking. World leaders will have to make good on the very public pledges they made in 2000 that "no country seriously committed to Education for All will be thwarted in its achievement of universal primary education by 2015 due to lack of resources." Action is also needed to strengthen the effectiveness of such assistance, especially by improving its predictability and availability to finance recurrent costs. Beyond EFA, helping countries accelerate development of higher-level skills needed to promote competitiveness and economic growth is a further priority for the Bank; and the Bank's 1999 education sector strategy is being updated to enhance the effectiveness of Bank assistance and its responsiveness to client needs.

Delivering the development promise of Doha

26. **Fourth**, for all countries success also hinges on the progress we can make this year on the Doha trade agenda. 2005 will be a milestone year for trade and development leading up to the Hong Kong Ministerial in December. At the moment the prognosis is not good. There are serious risks that the Doha process, even if concluded formally this year, will not achieve the initial ambitions for development. The trade talks have been largely inconclusive since last July's framework agreement revived the process, and in the worst case, that agreement could result in an outcome that achieves very little. The challenge of realizing the development promise of the Doha round is becoming increasingly daunting as we approach the Hong Kong Ministerial meetings.

27. As highlighted in the background note prepared for the Development Committee,¹ facing that challenge requires a serious increase in the level of ambition, centered on a transformation of agricultural trade policy in OECD countries, devoting greater attention to reducing the trade-restricting effects of non-tariff measures, and safeguarding and expanding the scope for developing countries to compete in services markets. Given trade restrictions on average are much higher in developing than developed countries, significant further liberalization by developing countries is also required to realize the full potential of trade for development. Middle income countries are likely to benefit most from liberalization of agricultural policies, but in turn will have to open up their markets and contribute to the gains for poorer countries more broadly. It will also be important to provide assistance to the poorest countries so that they can fully engage in the negotiations, and are able to meet commitments and undertake the necessary reforms and adjustment. We need to significantly expand "aid for trade" through technical assistance and support for capacity building and financial and other assistance to tackle behind the border constraints. And in all these areas we must act now if we are to have any chance of achieving a successful pro-development outcome in Hong Kong.

28. In the Bank we are providing practical help on a number of fronts, and will continue to do so, with an expanding work program aimed at helping developing

¹ *Aid for Trade: Competitiveness and Adjustment*, Joint Staff Note by the Staffs of the IMF and the World Bank.

countries exploit the potential gains from trade. There is a growing lending program for trade-related activities. Projected commitments for new trade operations in the FY04-06 period are significantly larger than in earlier years, with trade facilitation related lending becoming a major growth area. Comprehensive studies on how to improve trade policies and explore trade opportunities – in the context of the Integrated Framework for Trade Related Technical Assistance – have been launched in more than 35 countries in the past two-and-a-half years. These studies are complemented by regional studies that look at issues for several countries at a time. The World Bank Institute has also increased its training and capacity building in trade-related activities. We have given advice and assistance to a number of countries seeking WTO accession. And Bank financial support for trade-related operations has picked up significantly: fresh commitments for new trade-related operations are expected to reach US\$3.8 billion during the period FY04-06.

Increasing the effectiveness and amount of development assistance

29. **Fifth**, we need to act now to increase the amounts and quality of development financing. The Monterrey Consensus represented an important milestone in framing the financing for development agenda. Since then, there has been considerable work on both assessing financing needs and on the different options for mobilizing development finance. The separate note on *Financing the Development Agenda* and the background paper *Moving Forward: Financing Modalities Toward the MDGs* discusses the issues in more detail. Let me just highlight a few key messages.

30. Developing countries can and must do more to mobilize domestic resources – raising revenues through faster growth and better revenue administration, and releasing resources by improving efficiency in public spending. They must also build on progress in reforms that enhance their ability to attract private non-debt capital flows, especially foreign direct investment (FDI). In addition, many countries have been benefiting from stronger flows of remittances. Recent analysis in the Bank on the related issues of migration and remittances suggests that financial flows from remittances are now very substantial – possibly double the \$126 billion of recorded flows in 2004 – and further work is under way to improve data, assess net benefits and develop ways to strengthen integrity of transactions while reducing costs.

31. But while FDI, remittances and exports are important sources of foreign exchange, they are no substitute for official development finance. Aid and other forms of development finance play a critical and special role, providing resources to support the public policy reforms and investments needed to underpin successful private sector development, economic growth and enhanced delivery of human services – and hence progress in meeting the MDGs. As the analysis in the GMR makes clear, an increasing number of developing countries are significantly raising their capacity to absorb effectively substantial increases in aid – and with a little assistance others can similarly raise their absorptive capacity. I have little doubt that if we can double effective volumes of development assistance in the course of the next five years the resulting flows can be used and used well. Indeed, if we fail to do so we will be failing on the promise of the Millennium Summit and the series of commitments made at Monterrey and elsewhere.

As I see it, the world faces a series of challenges for the providers of development assistance – challenges that have to be met, and met now, if 2005 is to be a year of success rather than one of failure.

32. We must deliver on the promises of aid that have been already made; this is the most immediate and credible step to augment aid financing to meet the MDGs. If the commitments made at Monterrey and since to materialize, official development assistance will increase by around \$18 billion in real terms in the next two years to 2006. Delivering on that promise will be an important test of the commitment of the developed countries to do their part. Targeting this increased aid to where it is most needed is the next step, to the poorest countries for program and project expenditures needed to scale up progress towards the MDGs. Accounting of debt relief and donors' strategic and security objectives towards fulfilling ODA objectives will need to be agreed upon. To meet the test, this increased aid needs to be truly incremental aid to meet the real financing needs for the MDGs—for HIV/AIDS, for education, for water and sanitation, for roads and infrastructure.

33. There has been a welcome reversal in ODA following a decade of almost continuous decline, but with little incremental cash financing for the poorest countries. According to the Development Assistance Committee (DAC) of the OECD, ODA levels rose in nominal terms from \$52 billion in 2001 to \$68 billion in 2003 and to \$78.6 billion in 2004; in real terms, this represents a 4.3 percent rise from 2003 to 2004, following a 4.8 percent increase from 2002 to 2003 after taking into account inflation and the decline in the dollar's value. The total represents 0.25% of Development Assistance Committee (DAC) members' combined gross national income (GNI), the same level as in 2003. While the reversal in ODA commitments is noteworthy, the increase of aid to finance MDG needs in the poorest countries to date has been modest. The detailed breakdown for 2004 aid outcomes is not yet available, but as pointed out in the *Global Monitoring Report* the bulk of the \$8.5 billion increase in bilateral ODA during 2001-03 represents debt relief, technical cooperation, and other special purpose allocations including for strategic and security objectives, and the increase in flexible forms to finance project and program expenditure in recipient countries was a modest \$0.2 billion which was more than offset by exchange rate and price changes. We must not lose sight of the target of increasing aid to help countries meet the MDGs: that is the metric against which to measure success or failure.

34. In this context I very much welcome the successful conclusion of the fourteenth replenishment of IDA. I also applaud the policy directions staked out for the IDA14 period and appreciate the signal of trust in the Bank's commitment, our effectiveness in achieving results on the ground, and our expertise and experience. The commitment to a 30% increase in IDA 14 is indeed welcome, and while so far firm commitments only amount to a 20% increase, I hope that IDA donors can soon confirm commitments to make the 30% increase a reality. The enhanced resource envelope of IDA14 can provide an anchor for accelerating global efforts to meet the MDGs in the poorest countries. Additional financing from bilateral sources that could be linked with IDA operations

could help leverage the role of IDA and provide the financing needed to match country efforts to scale up investments and programs to meet the MDGs.

35. 2005 offers an important opportunity to raise sights higher for the future and to set goals on aid delivery, for example for 2010. Since Monterrey six countries have committed to meet the 0.7 percent ODA to GNI target in addition to the five that have already reached this target. Progress towards the 0.7 percent target must remain the central goal in mobilizing the concessional resources needed to meet the MDGs. While the short-term focus must be on delivering these immediate commitments, I believe we can and must raise the bar for the future. It is indeed gratifying that five new countries have adopted timetables for achieving the 0.7 percent ODA target. While I am acutely aware of the difficulties that countries face in raising their aid budgets, I hope that more countries will make 2005 the year in which they commit to joining or at least moving towards the 0.7 percent club.

36. We also need to continue to work on ways to increase the pool of resources for development through innovative mechanisms. 2005 provides an opportunity to make tangible progress on at least some fronts. Although the International Finance Facility may not be an applicable or feasible instrument for all donors, I hope that it will prove feasible for some, starting with the pilot program on immunization. I hope that we can take forward discussions on international taxes and other means to provide long-term financing for global public goods including development. I hope that we will put in place better mechanisms for mobilizing voluntary contributions: the public response around the world to the Indian Ocean tsunami disaster demonstrates the tremendous potential, but also the institutional challenges of private charity. And I hope that we can find ways to expand the scope of blending multilateral bank loans with bilateral grants to augment resources for tackling the MDG agenda in middle income countries. The Bank and the Fund are continuing to work on these options, but in the end it is governments – the member countries represented in this Committee – who have to decide whether or not to take them forward.

37. We need to address the issue of additional debt relief for the poorest countries. There are a number of proposals that have been put forward, and also agreement in the G7 to make progress. There are three main objectives that motivate the proposals for additional debt relief : (i) to reduce the debt overhang in low-income countries consistent with long term debt sustainability considerations, and end the “lend and forgive cycle”, which may cause some countries to stay in a continuous “debt trap”; (ii) to protect countries from exogenous shocks, which cause temporary payment difficulties as well as longer-term debt sustainability problems; and (iii) to provide debt service relief (equivalent to grants) until 2015 as a means to augment the financing for the MDGs. Additional debt relief can make a positive contribution for many of the poorest and most vulnerable countries. I see three main benefits: immediate resources that debt or debt service relief would provide for development needs; predictability that comes with the certitude of debt relief; and efficiency that comes with the flexibility and reduction in transactions costs.

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

39. Most important of all, we have to make aid more effective and more predictable. Improving the quality of aid is just as important as increasing its quantity. As highlighted in the *Global Monitoring Report* aid is often fragmented and volatile, not well aligned with country priorities, and entails high transactions costs. Fortunately, these issues are now receiving more attention and progress is being made, but it has been slow and uneven. As was requested by the Development Committee in its Communique of October 2004, the Paris Declaration, which was adopted by 90 countries and 27 development institutions, agreed on 50 commitments to improve the quality of aid, which will be monitored by 12 quantitative indicators.² Participants agreed to set targets for 2010 which can help track and encourage progress on implementing these commitments by donors and partner countries. Five preliminary targets were agreed upon: these will be reviewed, and 11 targets will be agreed upon by the time of the United Nations' five year review of the Millennium Declaration in 2005. The challenge ahead is to translate these agreements into results on the ground which will require concerted and cooperative efforts on the part of all. In country after country, and sector after sector, we have learned the power of aligning aid better with country priorities; strengthening and where possible using country budget and financial systems and processes; providing the assurance of predictable and flexible aid flows over a period of years so that countries can embark on long term programs, for example in education and health; and in some circumstances financing recurrent costs. Today only a very few donors are able to make medium-term aid commitments. I recognize that in many cases countries will only be able to implement this agenda in full if they can persuade parliaments to permit changes in the way their aid is delivered and accounted for. I hope we can agree on the importance of making the effort. Better alignment of aid with country priorities and the harmonization of aid practices should not be celebrated just in Mozambique, but should be the norm for all countries.

Addressing cross cutting, regional and global issues

40. While the focus of action must be at the country level, there are a number of challenges that cut across countries.

² *Paris Declaration on Aid Effectiveness: Ownership, Harmonization, Alignment, Results and Mutual Accountability*, Background Note for the Development Committee Meeting (DC2005-0002).

41. We need to focus on the **special development challenges in Africa**. The report, published last month, of the Commission for Africa chaired by Prime Minister Tony Blair contains a comprehensive analysis and set of recommendations. I am sure the Committee will want to discuss these at our meeting, and I know that the UK plans to make the report a focus for discussion at the G8 summit in July. The Bank has already strongly endorsed the report. I hope that we can all agree to try to advance its principal recommendations. In the Bank we have already started to assess the recommendations more closely over the next few months, and the implications for our own operations. The Bank has prepared a preliminary Indicative Action Plan for Africa that was considered by the Board. This Action Plan sets out options on how the World Bank Group can support faster implementation of the Monterrey Consensus in Africa, building on the achieved scaling up of Bank Group support to Africa since FY2000 and the Bank's Strategic Framework for IDA in Africa (SFIA). I very much hope that, based on further guidance from shareholders, and consultations with Africa's leadership and development partners, this action plan can provide the basis for strengthened World Bank Group's support to Sub-Saharan Africa.

42. Across all developing countries there are **massive needs for new infrastructure investment**, which will be critical in supporting achievement of the MDGs, poverty reduction and economic growth. Meeting the MDGs in Sub-Saharan Africa would require a doubling from about 4.7 percent of GDP in recent years to 9.2 percent over the next decade—implying annual spending on infrastructure of about \$20 billion and an associated need for additional external financing of about \$10 billion a year. Recognizing these needs, the Bank Group's Infrastructure Action Plan—launched in July 2003—committed us to re-engage in supporting infrastructure investments, rebuild country-level diagnostic work, and strengthen the Bank's instruments and approaches.

43. We are on track in implementing the Action Plan, and expect a sustained increase in our infrastructure business and results over the medium-term. In the first half of FY05, total lending commitments amounted to \$4.1 billion, doubling the amount for the same period in FY04, with commitments split almost evenly between IBRD and IDA, reflecting the massive demands in both low-and middle-income countries. We have also strengthened our analytic work, with greater emphasis on cross-cutting infrastructure diagnostics, working jointly with regional multilateral development banks. We are exploring options to allow the Bank Group to engage more effectively at the sub-sovereign level. And we are working with the IMF to find solutions to issues of limited fiscal space in client countries for infrastructure investments.

44. **Environment and climate change** is another key issue for 2005. The UK Presidency has pledged to make climate change a priority on the G8 agenda in 2005 as one of the most serious challenges of the 21st century. The Kyoto Protocol came into effect in February this year, and nations will begin discussions on future global action on climate change. The Intergovernmental Panel on Climate Change has estimated that a three degree Celsius change in global temperatures could lead to a loss of 2-9 percent of GDP in developing countries per year, as well as resulting in devastating effects on

human health and welfare, and fragile ecological systems. In the last decade, it is estimated that more than two billion people have been adversely affected by changes in climate: from South Africa to Central America, and from Bangladesh to Afghanistan, poor people bear the consequences of droughts and floods. To meet the challenge all countries, and especially developing countries, must integrate climate concerns into policy planning and improved governance in key sectors such as energy, water and transport.

45. The Bank Group is supporting the process in many countries through our own operations, with a focus on strengthening country policies and systems, and through the Global Environmental Fund (GEF) which we manage. We are also making a key contribution through the Bank's carbon finance business which leverages new and private investment into projects that reduce greenhouse gas emissions. We have more than \$410 million under management in six funds, including the Prototype Carbon Fund which is a public private partnership of 17 companies and 6 government entities pioneering the market in greenhouse gas reductions, the Community Development Carbon Fund that extends carbon finance to small scale projects, and the BioCarbon Fund that applies carbon finance to agro-forestry and land-use projects.

46. The effort to ensure **global financial stability** is a further continuing challenge. Bank-Fund cooperation remains central to the global efforts on crisis prevention and resolution. The joint Bank-Fund Financial Sector Assessment Program (FSAP) and the Reports on Observance of Standards and Codes (ROSC) are two central pillars of this effort. They provide a valuable framework for helping countries strengthen their financial systems and institutions, underpinnings that are critical to successful economic development and poverty reduction as well as to financial stability. In the five years since the programs were initiated, much has been accomplished. As of end-2004, about 120 countries – two-thirds of the membership – have participated in the FSAP program or agreed to participate in the near future. The ROSC exercise has also been remarkable, with 600 modules completed covering 120 countries from all regions of the world and at various stages of development.

47. For the future, the key task is to help countries implement systematic follow up to these assessments – to build capacity and institutions and to mobilize technical and financial resources for the task. Greater selectivity and tailoring of assessments to country circumstances is also called for, given the increasing participation in the program of smaller economies and lower-income countries whose financial systems present special gaps and development challenges. To this end, we are increasingly more targeted in our assessments, carrying out this work in collaboration with others; at the same time, we are focusing on core areas needed to inform the dialogue with member countries and to underpin Bank's lending and the Bank's country assistance strategies. In this context, I would like to thank the donors of the Financial Sector Reform and Strengthening Initiative (FIRST) which is already providing significant support to countries strengthening their financial sectors and following up from FSAP and ROSC assessments.

48. **Anti-money laundering and combating the financing of terrorism (AML/CTF)** also remains a special concern. Protecting national economies and financial systems against criminal abuse requires the adoption of highly elaborate and multi-sectoral prevention and control regimes. We have – with the Fund – proposed steps to support international efforts to curb money laundering, including through close collaboration with the relevant international bodies, notably the Financial Action Task Force (FATF) and the UN bodies. With agreement a year ago that AML/CTF should become a regular part of the Bank’s work and on the revised standard and its assessment methodology we have been working to expand our strategy for helping member countries enhance the integrity of public and private institutions through effective AML/CFT regimes, providing technical assistance to client countries through individual country and regional programs, and raising awareness through Global Dialogues. The Bank has thus far completed five assessments this year as part of the FSAP program, with two more underway. The Bank has also stepped up its TA activities as well as its collaboration with FATF-Style Regional Bodies (FSRBs).

49. There are a number of **other cross-cutting and global issues** where I believe the Bank must remain engaged because of their importance to development and relevance to our work at country level. Nearly half the people of the world today are under 25 years old; nine out of ten of these young people live in developing countries, and a billion of them will need jobs in the next decade. So **youth** is one such issue. **Disability** is another. Fighting poverty more effectively must include efforts to empower and utilize the human and economic potential of the 400 million disabled people in developing countries, most of whom are the poorest of the poor. Attention to disability issues is growing among client countries, an increasing number of them are now involved in inclusive education programs; India is the site of a major project on empowering disabled people. In 2004, Afghanistan, Bolivia, China, Ecuador, Kenya, and Uzbekistan have all requested assistance in conducting disability-related research. **Human rights** is a third issue. The Bank has long recognized that sustainable development requires *both* economic growth and social equity. There is, moreover, widespread recognition of the strong link between human rights and development. The connections between human rights and the attainment of the MDGs are also significant. The Bank’s work substantially contributes to the realization of rights of people in a number of areas, such as health, education, gender, participation, accountability, environment, institutional reform activities and, above all, the fight against poverty itself as a fundamental denial of human rights. Other Bank activities also contribute to the realization of human rights: these include fighting corruption, increasing transparency and accountability in governance. The Bank is currently reviewing its role with a view to making a more explicit link between human rights and our work, while at the same time remaining fully in compliance with our Articles of Agreement.

50. A final challenge for 2005 will be to respond effectively to the disaster that dominated the news as the year began. The **tsunami disaster** affecting countries in and bordering the Indian Ocean was one of the worst natural disasters in modern times. The damage in affected areas is extreme. Governments have responded effectively, and the support from donors, and private citizens round the world has been astonishing and

unprecedented. The Bank has been able to use its comparative advantages – in-house expertise on recovery and reconstruction, knowledge of the overall economies of these countries, sectoral knowledge from operations and analytic work, procurement and financial management skills, and experience with donor coordination and reconstruction financing – in assisting countries in formulating their recovery plans. Three principles have guided our efforts: the governments of the affected countries must have the central role and ownership; communities should be involved in assessing their needs and designing recovery programs; and the international community must act in coordination. As the needs assessments are completed, we will finalize work on emergency reconstruction credits and grants for the most affected countries that have asked for assistance: India, Indonesia, Maldives, and Sri Lanka. We expect to report back to the Board on the overall reconstruction efforts. Beyond the immediate relief efforts, it is clear that a concerted World Bank Group-wide effort, also involving IFC and MIGA, will be necessary to meet the broader reconstruction needs of the affected countries.

IV. ROLE OF THE BANK: STRENGTHENING THE BANK GROUP'S EFFECTIVENESS

51. Before turning to ways to strengthen our effectiveness as an institution, I should report briefly on developments in IFC and MIGA since the Committee's last meeting.

IFC

52. IFC has been making progress in implementing its strategic directions, including significantly strengthening its investment and technical assistance operations in Africa and implementing a new technical assistance facility to support private sector development in the Middle East and North Africa region with significant support from donors. In addition, the IFC has enhanced its strategic approach to technical assistance, with new monitoring and evaluation procedures and a new funding mechanism. Other internal improvements include a significant reduction in non-performing loans, a growing net worth, and improvements in risk management, human resources systems and environmental and social capabilities.

53. Looking forward, IFC will continue to perform a crucial role in infrastructure development (including public-private partnerships and municipal programs), in countries or regions not well-served by private sector finance, in innovative product areas such as housing finance, and by addressing critical needs related to the sustainability agenda, including enhancing the social impact of its projects and financing sustainable projects in energy efficiency, extractive industries and agribusiness.

MIGA

54. MIGA's business has been expanding steadily, with the outstanding portfolio now standing at \$5.5 billion. The agency has undergone significant changes in recent months, with a new business model that focuses on putting the agency on a financially and operationally sustainable path over the long-term. It centers on MIGA's unique role as a

multilateral risk mitigator, drawing on its governance structure to support development in ways that add value and complement the activities of others. This implies a focus on areas that public and private entities cannot serve as well, such as higher-risk markets, and other areas where MIGA has a unique comparative advantage. Underpinning the new model is a belief that proactive measures by MIGA can make a difference in terms of affecting investor perceptions and decisions about investment. Greater availability of information about investment opportunities and local operating conditions makes market entry decisions quicker and easier for investors. And attractive tools to mitigate risks – particularly those risks beyond an investor’s control – can make an important difference between whether investments take place and whether they do not.

Strengthening the Bank Group’s effectiveness

55. Given the scale of the challenges discussed above, I believe, and hope the Committee will agree, that the Bank Group is more important and more relevant than ever in the past. So it is more important than ever that we be effective and efficient in what we do. Chapter 6 of the GMR contains an assessment of the contribution being made by multilateral institutions, and many good suggestions for improvement. It also, rightly, stresses the importance of strong and effective cooperation and coherence between institutions. Let me set out my view on the Bank’s strategic direction for the future.

56. The Bank’s agenda, as I see it, is to contribute effectively, using our comparative advantages and working in partnership with others, to the challenges set out above.

57. The Bank’s poverty reduction mandate, coupled with the lessons we have gleaned from the growth experience of developing countries in the past decade, form the basis of a strategic framework that continues to be highly relevant for our work within countries, and in global programs. The twin pillars of the framework – **empowering people and promoting a favorable investment climate** – can help to identify priority areas for the Bank’s work. Further guidance on identifying strategic priorities is provided by a framework for selectivity within countries, across countries and for global programs. The major strategic challenge the Bank faces is one of implementation – across the continuum of client countries, in the mix of lending and non-lending services, in the degree of engagement, and in the choices of global programs and partnerships. In addition, key implementation challenges include the way in which we are organized and how we deploy our resources.

58. In our support to countries we must recognize the diversity in country circumstances and needs. The approach to development partnership and support is most advanced for low-income countries, with broad agreement that country-owned Poverty Reduction Strategies are the best means for more ambitious pursuit of development results. As noted, processes are underway to identify and give impetus to how the international community and the Bank can support development in middle-income countries and fragile states. There is a strong case for the Bank to remain engaged across the spectrum of developing countries, although the mix of services – knowledge, capacity

development and financing including its concessionality – will vary across and within these sub-groups of developing countries.

59. In addition, globalization and the need for global collective action have led to a growing agenda of global issues where the Bank is being asked to play both direct and catalytic roles. This includes long-standing agendas such as trade, debt relief, aid coordination and effectiveness, financial stability, and new ones such as migration and remittances, combating the financing of terrorism and climate change. In these and other areas, major international efforts are underway and the Bank is actively engaged based on its mandate and strengths. Much of these new demands is for knowledge and advisory services and not directly linked to lending.

60. As the GMR stresses, the breadth and interconnectedness of the development agenda on the ground and at the global level places a high premium on partnership and coherence. Accordingly the Bank has and is continuing to strengthen its collaboration with the IMF, the MDBs, the UN agencies, the WTO, other bilateral and multilateral institutions, with the private sector and with civil society organizations³. I have devoted much effort over the last few years in trying to strengthen these partnerships between institutions. I believe that across the Bank there is now recognition that we can do more by working as partners with others than we can by working alone. Although significant challenges remain, I believe this message is now taking hold across the international system. More than ever, successful development results depend on harmonization of efforts based on comparative strengths.

61. To further strengthen our effectiveness in addressing this agenda I see a range of areas where we need to continue to pursue an agenda for change.

- **Managing for Results** Effective delivery, quality and results are at the core of Bank's strategic objectives and are the focus of our management systems. There have been long standing efforts to improve delivery management, operational quality and aid effectiveness within the Bank. Between 1996 and 2004, the Bank reduced the average time for project preparation from 24 months to 16 months, and the rate of satisfactory project outcomes increased from 69 percent to 79 percent. The agenda on managing for results that was defined in the course of 2002 will help strengthen the Bank's contribution to the development community's efforts to sharpen the focus on development outcomes. This includes the adoption of results-based country assistance strategies and a results framework for IDA, supporting country demand and capacity to manage for results, addressing the need for better statistics to evaluate performance and results measurement, and fostering a global partnership on the results agenda.
- **Budget Reform.** While growing demands have been accommodated within a budget that has remained virtually flat in real terms over the past decade, a robust

³ The Presidents of the other MDBs and I have just sent the fifth *Update on Cooperation Among Multilateral Development Banks* jointly prepared by all the MDBs, to our Boards. The note highlights the important role that MDBs collectively play in the development architecture and the joint efforts to strengthen our contribution and effectiveness.

process for the examination of tradeoffs and appropriate flexibility in use of resources will be key in allowing the Bank to respond to evolving needs. To ensure that strategy drives resource allocation, we have put in place a major reform of the budget with more focus on performance management, clearer identification of trade-offs and simplified and streamlined processes. The three core principles of the reform are: (i) to strengthen the multi-year framework; (ii) to give management the flexibility and room to manage, and (iii) hold them accountable for performance. Business planning and monitoring processes will be simplified, and the focus of attention will gradually shift from hitting absolute targets at each fiscal year-end towards supporting continually improved management of resources in pursuit of medium-term goals. To strengthen accountability for decisions on strategy and use of resources, we are focusing on strategic performance indicators and embedding accountability in a multi-year framework that is better aligned with actual project time frames.

- **Improving Organizational Effectiveness** Over the past year, the Bank has undertaken a major review of how to strengthen its organizational effectiveness and its impact upon Bank operations. On the basis of the review, Management is proceeding with a number of recommendations including strengthening the Bank's delivery of client services and its work on global issues; simplifying internal planning and budgeting; and improving human resources management policies and practices. Some other recommendations on the more structural aspects will be considered following the current Presidential transition.
- **Governance.** To complement these steps, there may also be a need to consider ways to strengthen the Bank's governance system to further improve institutional effectiveness and to reflect modern practices, with clear accountability and benchmarks, and with appropriate representation of all stakeholders. The Committee continues to discuss issues of voice and participation, and while these are issues for shareholders and not management I do believe it is crucial to address them if in the longer run the institution is to retain the accepted legitimacy that is so important to its effectiveness. These are difficult issues that shareholders have been grappling with, and progress will be key to the long-term efficiency and effectiveness of the institution.

V. CONCLUSION

62. It has been a privilege to serve this remarkable institution for the last ten years. Over that time we have made some progress. I believe there is now a widely shared understanding of what needs to be done if we are to achieve our mission of eradicating poverty. It has also been a period of change at the Bank. There are further changes to be made, but the Bank is well placed to continue to contribute effectively to what has to be a global effort, in this critical year and in future. The Bank is a unique institution, with a superb and dedicated staff; its role in eradicating poverty and meeting our common aspirations for a better world for all has never been more important. I am confident that under the leadership of Paul Wolfowitz, the Bank will continue to rise to the challenge.