1

ADDRESSING POVERTY WORLDWIDE

A CHANGING ENVIRONMENT

The World Bank's client countries experienced a remarkable year, with average per capita gross domestic product (GDP) rising an estimated 6 percent in 2006. Even more significant, trends of sustained growth are emerging: annual per capita GDP growth in developing countries has averaged 3.9 percent since 2000, and 16 African countries—home to more than a third of the region's population—have enjoyed annual growth of more than 4.5 percent over the past decade. This growth has benefited the poor, with the number of people living in extreme poverty dipping below 1 billion for the first time since the Bank began measuring poverty, in 1990.

Clearly, developing economies are performing. Now is the time to meet that performance with increased aid. Donor countries have committed billions in debt relief and have met emergencies with well-timed assistance, thereby making an important contribution to the ability of poor countries to achieve their development goals. Further support could go beyond mitigating the burden of debt and disaster to enable performers to invest more in priority areas such as infrastructure, education, and health.

For many low-income countries, the development finance landscape has been transformed by unprecedented access to private capital—though that access is still uneven, with the poorest 51 countries receiving just 8 percent of the total in 2006. Meanwhile, traditional aid now comes from an abundance of donors, including some countries newly arrived at lending, and still others, such as foundations or even individuals, with highly specific goals. Taken as a whole, these are encouraging signs, especially when support aligns readily with national priorities.

This transformation underscores the vital convening role of the International Development Association, which serves as a cornerstone of the international aid system in many poor countries. IDA provides such countries with reliable aid support and leverages the assistance of other donors for coherent, country-owned programs and projects. IDA's efforts forge stronger partnerships between aid providers and recipient countries, leading to better outcomes for the poor.

The coming year will be crucial for IDA's clients, as donors will be confirming their commitments to the 15th replenishment of IDA. IDA15 will provide resources to assist the world's poorest countries from July 2008 through June 2011—critical years for developing countries trying to achieve the Millennium Development Goals (MDGs). Given the long lag time before development projects yield measurable results, IDA15 may be the last major opportunity for donors to support developing-country efforts to make significant progress toward achieving the MDGs by 2015.

For middle-income countries, access to market-based financing and risk-management tools continued to improve in fiscal 2007, as their costs of borrowing declined to near all-time lows. These countries require development partners that are flexible and responsive and that can provide a broad array of financing, risk-management, and credit-enhancement products, provided quickly and at lower transaction costs. International financial institutions, including the World Bank, must adapt to such changes in client complexion and outlook and to the constant changes in the global economic environment.

The World Bank uniquely must adapt to these changes while staying loyal to its vision: a world free of poverty. It pursues this end by focusing on its areas of comparative advantage, supporting client countries' pursuit of sustained and equitable economic growth. The Bank's support includes knowledge services, financial services, and strategy and coordination services. Additionally, the Bank advocates the adoption of prodevelopment policies around the world, particularly in relation to trade.

This report looks at the activities undertaken in the past fiscal year in the fight against poverty. The report pays special attention to Africa and focuses on five critical areas where the Bank can have a distinct impact: health, education, and gender; infrastructure and clean energy; financial and private sector development; governance and anticorruption; and in developing its strategy for middle-income countries.

HEALTH, EDUCATION, AND GENDER

Improvements in the areas of health, education, and gender are fundamental to achieving the Bank's mission: six of the eight MDGs address them, and complex interrelationships exist among the three. Progress in these areas requires vigilance, especially in Africa, where each has been highlighted as a flagship area for Bank support, in accordance with client country priorities.

Health, Nutrition, and Population

Across the world, poor people face high mortality rates, malnutrition, and limited access to reproductive and other basic health services. At the same time, millions fall into poverty every year as a result of illness. Health conditions are particularly dire in Africa, where no country is on track to meet the child mortality MDG.

Recent years have seen massive increases in international aid for health, with much of it targeted to specific diseases, such as HIV/AIDS (human immunodeficiency virus/acquired immune deficiency syndrome), tuberculosis, and malaria. However, relatively few resources have been provided to support health systems, and few institutions are in a position to bring donors, single-cause funds, and other sources together to help countries improve health outcomes. This is an area to which the World Bank is strongly committed and in which it has a comparative advantage. The Bank's updated strategy in health, nutrition, and population (HNP), discussed by the Board in April 2007, draws on the Bank's long experience in health financing, health systems, and cross-sectoral investments (box 1.1). Under the new strategy, lending in HNP will be even more closely tied to results than it has been in the past. The Bank will work across sectors and engage with a diverse group of actors to strengthen health systems and interventions, a necessary step for achieving improved treatment and prevention of any single disease. The Bank will also work

THE MILLENNIUM DEVELOPMENT GOALS

1. Eradicate Extreme Poverty and Hunger
Halve the number of people in extreme poverty, and the number of people who suffer from hunger, by 2015.

2. Achieve Universal Primary Education
Ensure by 2015 that all children will be able to complete a full course of primary education.

3. Promote Gender Equality and Empower Women
Eliminate gender disparity in primary and secondary education by 2005, and in all levels of education by 2015.

4. Reduce Child Mortality
Reduce by two-thirds the under-five mortality rate by 2015.

5. Improve Maternal Health
Reduce by three-quarters the maternal mortality rate by 2015.

6. Combat HIV/AIDS, Malaria, and Other Diseases
Halt the spread of HIV/AIDS, malaria, and other major diseases, and begin to reverse the spread, by 2015.

7. Ensure Environmental Sustainability
Halve the proportion of people without sustainable access to safe drinking water by 2015.

8. Develop a Global Partnership for Development
Further develop an open, rule-based, predictable, nondiscriminatory trading and financial system.

(See **www.developmentgoals.org** and **www.un.org/millenniumgoals**.)


to prevent poverty resulting from illness and to improve governance, accountability, and transparency in the health sector.

Lending for HNP, including health financing, reached $1.83 billion in fiscal 2007. Health systems performance was a dominant theme in fiscal 2007, representing $739 million in new lending. Support to population and reproductive health programs totaled $303 million, and support to the treatment and prevention of HIV/AIDS reached $300 million.

The Bank has long supported health-related projects in countries such as Argentina, Ghana, Mozambique, and Tanzania, where a wide range of lending approaches has been used over time. Bank assistance has also had a positive effect in postconflict countries (box 1.2). For example, in Afghanistan and Timor-Leste, armed conflict resulted in huge losses in health personnel, infrastructure, and management capacity. Consequently, the countries turned to civil society organizations to provide basic health services. As conflict died down, both governments developed new strategies to integrate public and nonstate health service providers using robust monitoring and contracting approaches. Bank financing for HNP and other sectors, as well as support for public financing reforms, helped the governments implement these strategies. In Afghanistan, the immediate result has been a fourfold increase in the use of health services in target provinces. In Timor-Leste, the average use of health services increased from one annual visit per person to at least two-and-a-half visits. Measles immunizations rose from 26 percent to 73 percent of children, and skilled attendance at birth increased from 26 percent to 41 percent.

Most of the analytic work and technical assistance the Bank provided in fiscal 2007 concentrated on health systems issues. Two reports, *Health Financing Revisited* and *Beyond Survival,* summarize global lessons in health financing and provide policy recommendations based on the specific economic, political, and institutional conditions countries face.

Education

The World Bank is the world's largest source of external investment support for improving education in middle- and low-income countries, having transferred about $40 billion in loans and credits for education since it started lending to the sector in 1963. This represents nearly 7 percent of total lending over that 44-year period. As with health, the Bank has a unique ability to consult with national governments, United

BOX 1.1 HEALTHY DEVELOPMENT: THE WORLD BANK'S STRATEGY FOR ACHIEVING HEALTH, NUTRITION, AND POPULATION RESULTS

The World Bank's new strategy for health, nutrition, and population aims squarely at helping developing countries strengthen their health systems and ensure synergies between those systems and priority programs (for example, programs focused on HIV/AIDS, malaria, tuberculosis, nutrition, and reproductive health). By strengthening health systems, the strategy aims to boost economic growth, reduce poverty caused by catastrophic illness, and provide cohesion among the multiple health-related programs within client countries.

The strategy underwent an extensive consultative process with 9 client countries and 65 global partners, including civil society organizations and bilateral and multilateral organizations. The following strategic objectives emerged from that process:

- Improve measurement and outcomes of health-related MDGs
- Prevent poverty caused by illness by improving financial protection
- Support the contribution that good health and sound health-system policy can make to economic growth
- Improve governance, accountability, and transparency in the health sector

The new strategy maintains the Bank's unswerving commitment to achieving results on the ground and to improving the health conditions of people in client countries, particularly the poor and the vulnerable. (See **www.worldbank.org/hnp**.)

Nations (UN) agencies, bilateral agencies, donors, civil society organizations, and other stakeholders to support developing countries in their efforts to provide education to all their citizens as a means to empower them and to boost economic growth.

Education lending in fiscal 2007 reached $2 billion. The Bank provided about $1.6 billion in IDA funding, an all-time high. Aid to Africa—which had declined steadily over the past five years to a low of $339 million in fiscal 2006—reached $707 million, nearly all from IDA, in fiscal 2007.

The Bank approved 28 education projects in fiscal 2007. These included $280 million for vocational and technical education in India; nearly $250 million for two projects in Nigeria aimed at increasing access and learning in primary schools and at improving the quality of higher education;

BOX 1.2 RAPID RESPONSE

The Bank has responded to a growing number of emergency situations in recent years. It has helped countries recover from natural disasters, such as the 2004 tsunami in the Indian Ocean and the 2005 earthquake in Pakistan; it has supported reconstruction in postconflict situations; it has helped to avert outbreaks of pandemics, such as the avian flu; and it has responded to manmade disasters, such as oil spills. The 2006 report by the Independent Evaluation Group, *Hazards of Nature, Risks to Development,* noted that although there have been many successes, the Bank's response has often lacked the speed and effectiveness that emergencies demand.

To address these issues, the Board approved a new policy framework in February 2007 for rapid response to emergency and crisis situations. The new framework allows the Bank to act more quickly by acknowledging the wide range of situations encompassed by the terms *crisis* and *emergency* and by simplifying procedures and requirements in emergency operations. The new framework addresses constraints faced in the early (and often critical) stages of recovery and establishes a basis for the Bank to work with countries to reduce the risk of crises and disasters in the first place.

To support implementation of the new policy, the Bank drew on staff from across the institution with experience in emergency work. As soon as the new policy framework took effect, task teams began to implement it. The new policy was first applied to imminent crises. The Emergency Social and Urban Rehabilitation Project, in the Democratic Republic of Congo, was the first project to receive approval under the new policy. The project addresses the escalating risk of crisis in that country. Four other projects were subsequently approved under the new policy in fiscal 2007.

At the global level, the Bank is working with the United Nations on a framework fiduciary agreement to facilitate World Bank–United Nations collaboration during crises and emergencies. In addition, as part of the effort to reduce the risk of disaster in high-risk countries, the Bank has joined with other donors and the United Nations in creating the Global Facility for Disaster Reduction and Recovery, which will help countries develop and implement disaster risk–mitigation strategies and will provide funds for reconstruction. (See **www.worldbank.org/hazards**.)

$150 million for postconflict support for education in the Democratic Republic of Congo; and $80 million for decentralizing education in Kenya.

Because education's role in broadly shared growth is complex and pervasive, 79 investment projects or development policy operations approved in fiscal 2007 contain funding to support education. For this same reason, the Bank's approach to education has often involved addressing problems outside education that hinder development of the sector. Reducing or eliminating school fees, addressing HIV/AIDS in schools, and devolving decision making and funding to schools and parents are examples of reform priorities that require a cross-cutting approach.

Seven low-income countries—Benin, Cambodia, Mali, Mauritania, Mongolia, Mozambique, and Sierra Leone—received a total of $265 million in grant support under the Education for All Fast-Track Initiative (FTI) in fiscal 2007. The FTI is a global partnership between donor and developing countries that helps to provide increased, better coordinated, and more effective aid to countries with sound education plans. These grants were made under the FTI Catalytic Fund, a multidonor trust fund managed by the Bank that provides transitional financial assistance to countries whose education sector plans have been endorsed under the FTI process but that have difficulty mobilizing sufficient external funding. Thirty-one countries are now endorsed by the FTI.

Fiscal 2007 saw other encouraging results. Worldwide, the number of primary-school-age children out of school has fallen from about 100 million in 2000 to an estimated 77 million in 2006, and the ratio of girls to boys in primary schools is rising rapidly in many countries (box 1.3). The greatest increases

BOX 1.3 PUTTING 550,000 MORE CHILDREN IN PRIMARY SCHOOL IN BURKINA FASO

Burkina Faso's primary school enrollment rate was among the lowest in the world in the 1990s. Enrollment was very low in rural areas, where children, particularly girls, were kept at home because of the distance to school, the high cost of schooling, and the high opportunity costs for poor families whose children contributed significantly to family income.

To address the problem, IDA brought $32.6 million to a $110 million program supporting the government's Basic Education 10-Year Program. Just as significantly, it provided a framework that harmonized support from all partners—Belgium, Canada, Denmark, the European Commission, France, the Netherlands, Sweden, UNICEF, and nongovernmental organizations—through a common-basket fund that allowed effective allocation of project resources.

The first phase of the program, completed in fiscal 2007, improved access to primary education in rural areas by constructing and rehabilitating schools and financing equipment and facilities. It also supported curriculum development, teacher training, and capacity building within the Ministry of Basic Education, paying particular attention to financial management, budgeting, procurement, monitoring, evaluation, and donor coordination.

As a result of the program, an additional 550,000 children have since been enrolled in primary school. Gross enrollment rates nationwide increased to 62 percent (55 percent for girls) in 2006, up from 42 percent (36 percent for girls) in 2000. In the 20 most underprivileged provinces, enrollment rose to 47 percent (41 percent for girls) from 30 percent (24 percent for girls) over the same period.

IDA will continue to support the government's 10-year program to ensure that the foundations laid for the reform will be strengthened over time. A Post-Primary Education Project that builds on the current operation is being implemented to address access and equity in secondary education. (See **www.worldbank.org/burkinafaso**.)

in enrollments have occurred in South Asia. Bangladesh has raised gross primary enrollment rates to almost 100 percent and has already met the MDG on gender parity in school enrollment. These hopeful signs suggest that globalization can work in support of shared growth in the countries that continue to invest in education.

In addition to investment support, the Bank continues to produce sector analyses and cross-cutting analytical reports that raise local awareness and increase global knowledge. More than 30 education sector papers or strategy documents were prepared in fiscal 2007, and numerous Poverty Reduction Strategy Papers addressed education. Feedback from governmental counterparts and nongovernmental actors indicates that the Bank's policy advice and global knowledge base are at least as important as its financial support.

A redoubling of efforts will be required in education in fiscal 2008 and beyond. Only 25 of 81 IDA-eligible countries have achieved or are on track to achieve universal completion of primary school by 2015 (the second MDG). Bank support for reaching this goal, including support through the interagency FTI, has mostly emphasized increased access, according to an Independent Evaluation Group (IEG) analysis from fiscal 2007. Although the Bank was widely successful in increasing enrollment and access, problems with student dropout and learning outcomes remained. IEG recommended that future Bank support increase the emphasis on learning outcomes and on improved system management and governance and that the Bank work with FTI partners to reorient the initiative. Since that evaluation, all new primary education projects have been reviewed for attention to learning outcomes; programs of analysis, training, and policy dialogue have been organized around the theme of learning outcomes and assessment; and the Bank has engaged its FTI partners in building learning outcomes into the initiative. Measuring learning results and benchmarking them against local and international standards will help link countries to the global economy. (See **www.worldbank.org/education**.)

Gender Equality

The Bank has a strong comparative advantage in the promotion of gender equality. The Bank's analytical capacity puts it in a good position to make the business case for gender equality and to document how increased gender equality can accelerate shared growth. Operationally, the wide sectoral scope of the Bank's lending means that it is able to take advantage of many entry points—ranging from health and education to financial markets and infrastructure—to promote gender equality.

During fiscal 2007, the Bank adopted an action plan to empower women economically. The plan, "Gender Equality as Smart Economics," launched operations in all developing regions. These operations included new activities targeting agriculture, private sector development, financial services, and infrastructure to help increase the productivity and earnings of women producers.

In Tanzania, where women have very poor access to financial services, the plan has established a line of commercial credit for women through a local bank. The program is providing training to women to increase their "bankability," and it is supporting regulatory reforms to give women better access to credit. This project and others under the gender action plan can facilitate women's transition to good-quality employment; can increase the number of women starting agribusinesses and engaging in high-value agriculture; and can boost women's access to essential infrastructure services, particularly transport, water, and energy.

The Multi-Country AIDS Project for Africa has focused particular attention on addressing gender dynamics in its response to the pandemic. In Chad, IDA funds a project to reduce the transmission and socioeconomic impact of

HIV/AIDS by supporting education and income-generating activities for women. In Rwanda, IDA has financed access to antiretroviral care for 5,000 poor rural people, most of them women. In Africa generally, IDA has financed services to prevent mother-to-child HIV transmission for more than 1.5 million women and has helped distribute 1.3 billion male and 4 million female condoms.

The focus of the Bank's *Global Monitoring Report 2007* was on gender equality and on the progress of member countries in meeting the related official MDGs. The report identified gaps and developed a set of complementary indicators to strengthen gender-equality monitoring.

Financial support from the governments of Canada, Denmark, Germany, Norway, Sweden, and the United Kingdom continues to encourage innovation in the mainstreaming of gender issues in the Bank's work. (See **www.worldbank.org/genderequality**.)

INFRASTRUCTURE AND CLEAN ENERGY

Infrastructure

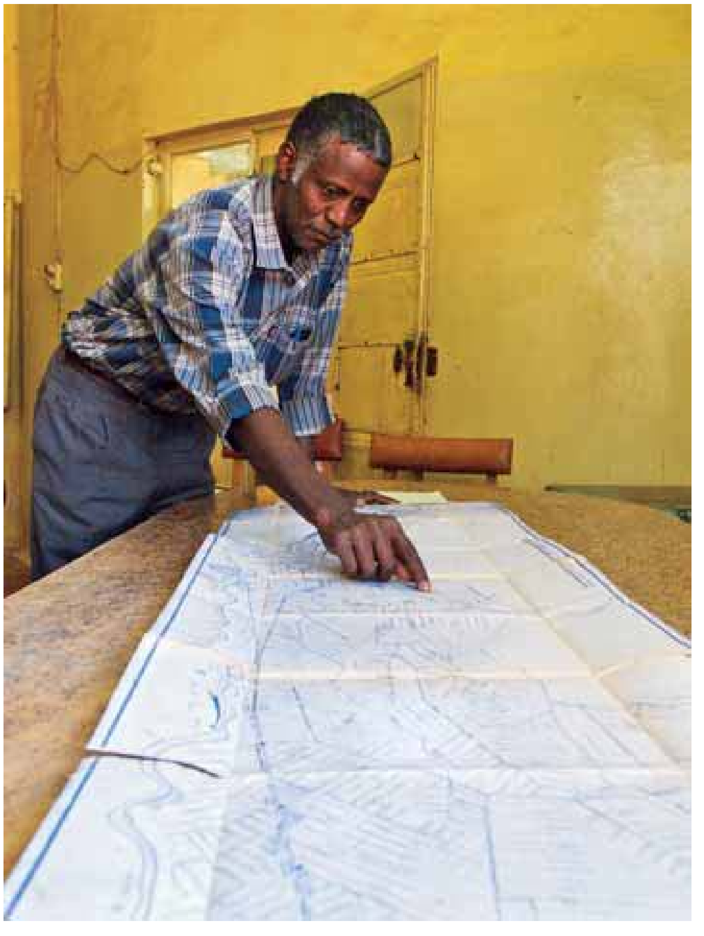
Improving infrastructure in developing countries is key to reducing poverty, increasing growth, and achieving the MDGs. Leaders of developing countries often say they need not only more and better infrastructure facilities and services but infrastructure that is environmentally sound, socially accepted, and financially sustainable.

By building on the increased investment opportunities available under the Infrastructure Action Plan and by integrating the lessons learned in its long involvement in infrastructure worldwide, the World Bank has remained a leader in working with developing countries in this area. It assists them in providing the basic sustainable infrastructure capacity and services needed for permanent poverty reduction.

The Bank increased commitments involving infrastructure to $9.9 billion in fiscal 2007, a 24 percent increase over the previous year. Transport remained the largest component, with $4.9 billion in lending (50 percent of the total), followed by new water and sanitation commitments of $3.1 billion (31 percent of the total).

The Bank supports activities in a wide range of infrastructure services, including energy, transport, water supply and sanitation, urban services, land use management, and information and communication technologies. A key area of involvement in the last year has been the promotion of clean energy investments to help the international community deal with growing threats from global warming and climate change (see "Clean Energy," below, and box 1.4).

The Bank provides financial assistance for investment projects; leverages financing from donors and the private sector; and engages in policy dialogue and provides advice



on sector reforms, working with country partners to build and strengthen institutions. The Bank's infrastructure agenda is particularly relevant to Africa, where 300 million people lack access to improved water sources, 450 million people lack adequate sanitation services, and transport costs are among the highest in the world.

The continued growth in lending was accompanied by an organizational realignment that saw infrastructure units within the Bank integrated with units working on the environment, agriculture and rural development, and social development. The result was the creation of a robust Sustainable Development Vice Presidency charged with ensuring that Bank infrastructure programs yield the kinds of environmentally and socially sustainable programs that countries need and request.

A report produced by the former infrastructure unit—*Infrastructure at the Crossroads: Lessons from 20 Years of World Bank Experience*—foreshadowed the integration by exploring the importance of integrating environmental and social dimensions into project identification, preparation, appraisal, and supervision, and of allocating sufficient resources to mitigate any adverse impacts of development.

IEG has been actively reviewing the Bank's work in infrastructure in fiscal 2007. A recent IEG evaluation of Bank assistance to the transport sector concluded that past performance has generally been effective but that the focus on rural and intercity roads is insufficient because of the rapidly growing impact of urbanization and globalization. More emphasis needs to be given to the reduction of urban

BOX 1.4 ADDRESSING THE RISK OF CLIMATE CHANGE IN KENYA

The number of people affected by droughts and floods in Kenya is doubling every decade. To help poor people deal with the impact of such climatic shocks, IDA funded two phases of the Arid Lands Resource Management Program. The program has been successful in addressing short-term impacts of climate variability and is now focusing on addressing the longer-term impacts of climate change.

Climate models project a substantial increase of up to 5 degrees Celsius in the annual average temperature for Kenya by the end of the century. While uncertainties remain regarding the changes in average rainfall, projections clearly indicate a growing risk of both dry spells and intense precipitation events. Recognizing this, IDA provided an additional $60 million in financing in fiscal 2007 to deepen and broaden the government's efforts to address climate variability, and the Global Environment Facility is contributing an additional $5 million in fiscal 2008 to deal with these risks. The next phase aims to increase institutional capacity to plan for climate change by improving information flows and analytical capacity; to promote public and private investment through incentives for appropriate investment; and to increase community resilience by piloting and demonstrating alternative livelihood options through community-based microprojects. (See **www.worldbank.org/kenya**.)

traffic congestion, vehicle emissions, and accidents. IEG also looked at management of agricultural water. Effective management is vital for feeding growing populations and for managing competition from urban regions for limited water resources. IEG called for greater attention to the role of agricultural policy and trade in alleviating regional water shortages, and it encouraged the Bank to demonstrate the impact of sound agricultural water management on poverty reduction, employment, and health. (See **www.worldbank.org/infrastructure**.)

Clean Energy

Increasing access to safe, modern, and economical energy in developing countries, and working to ensure that this energy is as clean as possible, is a major and growing field of activity for the Bank. As a leading international organization with the financial, technical, and human capacity to work throughout the developing world, the Bank is in a unique position to help countries accelerate their use of clean energy for sustainable development. The Bank has consistently surpassed the target it set for itself in 2004 to increase its annual investments in energy efficiency and new renewable energy by an average of 20 percent between fiscal years 2005 and 2009. In the first two years of that commitment, investments in new renewable energy and energy efficiency totaled $1.13 billion, more than double the target of $552 million over the two years.

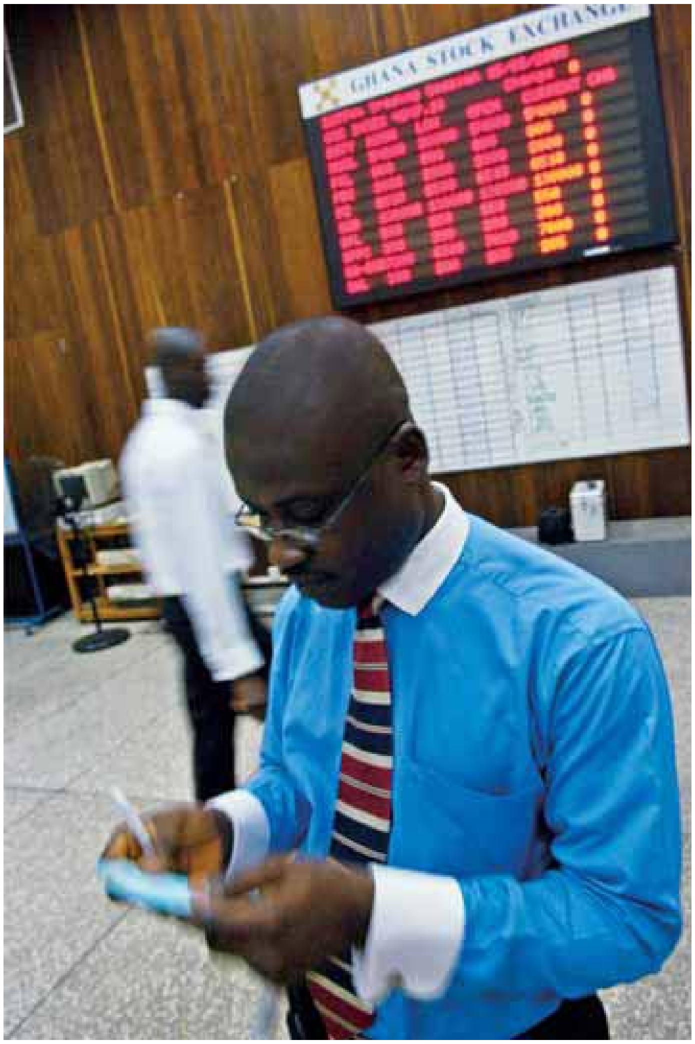
Additionally, the Bank is developing a Clean Energy Investment Framework, which addresses three interrelated issues: accelerating investments that help increase supplies of clean energy for development and improve access to affordable energy for the poor, particularly in Africa; promoting the transition to a low-carbon economy; and assisting developing countries as they adapt to the inevitable impact of climate variability and change.

Total energy support from all sources—including the Bank Group, the Carbon Finance Unit, and the Global Environment Facility—is expected to exceed $10 billion in the three-year period beginning in fiscal 2006, up from $7 billion over the previous three years. Furthermore, an action plan in support of the Clean Energy Investment Framework will encourage the expansion of African initiatives that aim to increase the number of households with access to modern energy from 25 percent today to 35 percent by 2015 and to 47 percent by 2030. The plan also aims to support the transition to a low-carbon economy—especially in Brazil, China, India, Mexico, and South Africa—by increasing analytical, knowledge, and investment support. The plan also seeks to assist countries as they adapt to climate variability and change by providing for analytical work and for development of risk-management instruments and other tools and methodologies. The goal is not just to increase investments but to "climate proof" them as well.

IEG assessed a subset of the Bank's clean energy portfolio—that is, new and renewable energy—in fiscal 2007 and found its work responsive to the needs of developing countries and in agreement with the Bank's overall energy strategy. In its review, IEG recommended that the Bank continue to support investment climates conducive to commercialization of new and renewable energy and to make allowances for the long periods often required for adoption of renewable energy sources. IEG further recommended that the Bank strengthen the monitoring and evaluation of its renewable energy projects. The review encouraged the Bank to support new and renewable energy in country and energy sector strategies. (See **www.worldbank.org/infrastructureandcleanenergy**.)

FINANCIAL AND PRIVATE SECTOR DEVELOPMENT

The financial and private sectors play a central role in meeting the World Bank Group's development mission. Deep, efficient, and well-regulated financial markets and a good legal and regulatory environment for the private sector give firms—from microenterprises to multinationals—the opportunity to invest productively, create jobs, and grow. Well-functioning markets play a key role in helping poor people rise out of poverty by leveling the playing field of opportunity for would-be entrepreneurs and employers and by providing poor households with improved opportunities to earn incomes, save, obtain credit, and buffer themselves against hard times. Efficient markets are especially needed



in Africa, where financial and private sector development is uneven; the burden of business regulation is excessive; access to finance is limited, especially in rural areas; and financial intermediation is less widespread than in any other region in the world.

Until this year, the Bank maintained separate networks for private sector and financial sector development. In view of the close ties between the two, the networks were merged in fiscal 2007 to create a central vice presidency for Financial and Private Sector Development (FPD). FPD is a joint Bank-IFC-MIGA vice presidency, and the Vice President leads the coordination of Bank and IFC technical assistance to governments in support of financial and private sector development. The new vice presidency focuses on creating the institutional foundations for effective markets, promoting open and competitive markets, and supporting social safety nets using market-based approaches.

The Board discussed a new financial strategy in April 2007. The strategy identifies important changes in the Bank Group's business environment that necessitate changes in its strategic focus, in the model for its advisory services, and in the allocation of Bank and IFC support. The Bank Group has extensive country and global knowledge of the microfoundations of effective financial markets and institutions. Its investments and advisory work offer unique insights on how financial issues play out in sectors ranging from agriculture to health care. The Bank Group is thus well-placed to see all aspects of financial reform within the broader economic development agenda. This expertise enables it to engage at a practical level with countries in reform and to provide a development voice in international standard-setting bodies. In keeping with this comparative advantage, areas of special focus going forward are the development of market infrastructure (such as contract rights and enforcement, payments systems, credit information systems, and disclosure standards); prudential oversight (compatible with better risk management and wider access to financial services); and targeted initiatives to improve access to finance for the underserved and to develop domestic capital markets.

Using information—rather than loans or conditionality—to promote change, the *Doing Business* report, a joint Bank-IFC publication that is published annually, informs governments in 175 economies on how regulations help or hinder businesses in their countries. Since the project's inception in 2003, more than 70 regulatory reforms have been inspired or informed by *Doing Business*, making it easier to start, run, or close down businesses around the world. In addition to the *Doing Business* report, a series of subnational reports published in fiscal 2007 covered states and cities in Bangladesh, Brazil, India, Mexico, and Pakistan.

Complementing the *Doing Business* analysis are enterprise surveys, through which the Enterprise Analysis unit seeks to obtain firm-level views on constraints to doing business. By the end of fiscal 2007, the unit had surveyed 65,000 firms in more than 90 countries. Additionally, the unit piloted a new instrument in fiscal 2007 to survey businesspeople in the retail, microenterprise, and information technology sectors in India.

The Bank continues to assess corporate governance and to assist countries in improving their corporate governance practices. In fiscal 2007, it completed nine corporate governance reviews, including four corporate governance Reports on the Observance of Standards and Codes, four

reviews of governance at state-owned enterprises, and one review of corporate governance in the banking sector.

Fourteen financial sector assessments were completed under the joint World Bank–International Monetary Fund Financial Sector Assessment Program in fiscal 2007, including six second-round assessments (updates). To perform assessments, staff from the Bank and the Fund—assisted by experts from cooperating official agencies—conduct a comprehensive peer review of a country's financial system. This review helps countries prioritize appropriate policy responses to discovered vulnerabilities. The assessment teams also highlight opportunities for improving the sector's ability to promote sound economic development. The pipeline for fiscal 2008 indicates that demand for the program continues unabated.

During fiscal 2007, FPD established a program to develop financial markets that would help households deal with risk. The program—Financial Markets for Social Safety Nets—addresses housing finance, funded pensions, and insurance. The housing finance unit helped increase access to housing finance for lower-income households and expanded residential mortgage markets through loans, grants, and advisory services in all regions. The pension unit prepared reports on the Brazilian and Czech pension systems, which the relevant governments can use to strengthen the case for reform. The insurance unit supports the provision of health, life, livestock, and crop insurance to the poor; such programs are already active in Africa, East Asia, and South Asia. The Financial Markets for Social Safety Nets Program is currently supervising $2.5 billion in Bank loans and is supporting preparation of new loans worth $1.5 billion.

FPD continues to invest in Web sites, training programs, case studies, and how-to guides in order to share knowledge. Five practitioner toolkits were published in fiscal 2007 on licensing, alternative dispute resolution, public-private dialogue, inspections, and business registration.

FPD also partners with institutions outside the World Bank Group to further its mission. The Foreign Investment Advisory Service (FIAS)—funded by the Bank, IFC, and MIGA, together with several donors—helps developing countries improve their business environments in order to increase private sector activity and investments with positive development impact (also see page 62). The Consultative Group to Assist the Poor—a 33-member, independent institution housed at the World Bank—works with financial institutions, ratings agencies, governments, funders, and others to promote microfinance. FPD also promotes better corporate governance in private sector companies through the Global Corporate Governance Forum. This multidonor trust fund was cofounded by the World Bank Group and the Organisation for Economic Co-operation and Development (OECD) to promote local, regional, and global initiatives that improve the institutional framework and practices of corporate governance. FPD manages the Financial Sector Reform and Strengthening Initiative (FIRST), which donors pledged to continue supporting through 2012. FIRST promotes stable, deep, and diverse financial sectors by providing grants. Since it was set up in 2002, the initiative has supported about 220 technical assistance projects in the financial sector.

The Bank sharpened its focus on fighting money laundering and the financing of terrorism in Africa this fiscal year. A parliamentarian forum, organized with the Global Organization of Parliamentarians Against Corruption, provided parliamentarians—the majority from Africa—with a forum in which to discuss challenges associated with fighting corruption, money laundering, and terrorist financing. The Bank also funded several multiyear comprehensive technical assistance programs in Africa that seek to develop systems that protect market integrity without hampering access to finance. (See **www.worldbank.org/finance**.)

STRENGTHENING GOVERNANCE AND REDUCING CORRUPTION

Improving governance and fighting corruption helps countries to better deliver basic services and to create growth and employment opportunities for the benefit of the poor. This work is therefore fundamental to the Bank's mission. In March 2007, the Board unanimously endorsed a new strategy on Bank engagement on governance and anticorruption. Under this strategy, the Bank will expand and strengthen its support for improving governance and curbing corruption in order to fight poverty; improve the delivery of services; strengthen the environment for private investment; and foster economic growth at the project, country, and global levels (box 1.5).

Activities at the Project Level

Governance and anticorruption are being addressed at the project level across the Bank's portfolio, including in public sector reform, infrastructure, health, extractive industries, and the financial sector. In fiscal 2007, World Bank support to governance was $3.8 billion—$3.4 billion to public sector governance and $424 million to support the rule of law. This comprised 15 percent of Bank lending.

BOX 1.5 THEMES OF THE BANK'S NEW GOVERNANCE AND ANTICORRUPTION STRATEGY

Agreement on the Bank's governance and anticorruption strategy was the result of a systematic consensus-building process. A draft strategy was presented to the World Bank–International Monetary Fund Development Committee at the Annual Meetings in Singapore in September 2006. Between November 2006 and January 2007 the Bank held consultations with a range of stakeholders—including governments, civil society, the private sector, and multilateral and bilateral development partners—in 35 developing countries and 12 donor countries. The Bank also participated in four global events and solicited online feedback, reaching more than 3,200 stakeholders worldwide.

Key messages from these consultations included the following:

- Stay engaged, even in poorly governed settings
- Engage not just with governments but with a range of stakeholders, including legislatures and the judiciary, the private sector, civil society, and the media
- Strengthen country systems—such as public financial management, procurement, regulatory, legal, and administrative frameworks—to fight corruption
- Increase the emphasis on disclosure, participation, and third-party monitoring of Bank operations
- Harmonize the Bank's actions with those of donors and other actors
- Enhance monitoring and evaluation of the Bank's governance and anticorruption activities through the use of disaggregated or "actionable" indicators of governance

This process brought about a strategy that identifies mechanisms to build transparent, accountable, and capable states; outlines instruments to improve monitoring and curb corruption in projects the Bank funds; harmonizes the Bank's efforts with those of other development partners; and encourages collaboration with the range of development actors. (See **www.worldbank.org/governance**.)

Assistance for governance includes support for increasing transparency in public financial management, strengthening tax and customs administration, enhancing civil service performance, supporting legal and judicial reforms, and enabling local and central governments to deliver services more effectively and with greater accountability to local communities. A project in Afghanistan is funding improvements in procurement and financial management. In Cambodia, the Bank is supporting more transparent civil service pay structures. In the difficult postconflict environment of Liberia, the Bank, under the multidonor Governance and Economic Management Action Plan, helped streamline budget execution processes and fiduciary controls while building capacity. By providing Institutional Development Fund (IDF) grants, the Bank has helped strengthen the capacity of Mexico's Federal Institute for Access to Information. IDF grants have also allowed the Slovak Republic to redesign and streamline the judicial system and increase access to justice.

The Department of Institutional Integrity (INT) investigates allegations of corruption involving Bank operations and possible staff misconduct. The Bank offers multiple outlets for reporting allegations of fraud, corruption, and other misconduct in Bank-financed projects, including an international hotline (+1-800-831-0463). In fiscal 2007, INT released the *Integrity Report of the World Bank Group, Fiscal Years 2005–2006*, which details actions the Bank has taken in investigating fraud, corruption, and other misconduct over that period. The programmatic elements of a new Voluntary Disclosure Program were approved by the Board in August 2006 to elicit voluntary cooperation in the fight against corruption from firms that have previously engaged in wrongdoing. Information on the companies and individuals the Bank has sanctioned is publicly available on the Bank's Web site.

An independent panel was established to review INT's roles, responsibilities, and working relationships as part of the Bank's governance and anticorruption strategy.

Activities at the Country Level

Improving governance has become a component of the Bank's country assistance strategies (CASs) in most countries, and it is a central element in some, including those of Albania, Bangladesh, Indonesia, and several countries in Africa. Bank support for governance is channeled through a mix of lending, grant, analytical, and advisory instruments.

Consistent with its heightened focus on governance, IDA makes its allocations based in large part on country performance ratings, and two-thirds of the value of this rating is based on a country's governance. Research over the past two decades has shown that governance has a strong impact on both development performance and aid effectiveness. The global commitment to reducing poverty by increasing aid—supported by IDA—is based on the principle of mutual accountability: more aid is provided the greater the effectiveness of how aid is used. Aid is best increased using recipient country systems for public policy making, budgeting, and service provision.

The World Bank Institute, the knowledge-sharing and learning arm of the World Bank, promotes the Bank's governance and anticorruption agenda through its Global Governance Program. The program delivers courses and seminars, provides governance advisory services, and carries out operational research on various aspects of governance. These activities and diagnostic tools help support action planning for in-country reform. In fiscal 2007, the program published an updated set of governance indicators for 213 countries and territories. In partnership with bilateral agencies, local authorities, and civil society, the program is supporting in-depth governance and anticorruption diagnostic studies in Benin, Burundi, El Salvador, and Haiti; it is planning to complete studies in Kenya and Nigeria; and it has received preliminary requests for diagnostic-related assistance from 11 other client countries.

IEG finds that the bulk of the Bank's assistance in governance and anticorruption has taken the form of reform programs in public administration and public financial management. This assistance has often improved the quality of public sector management processes without translating into improvements in the perceived quality of governance. Yet recent progress in Eastern and Central Europe shows that it is possible to raise perceived quality in a limited time when there is strong country commitment to doing so. The IEG evaluation suggests that public sector reform initiatives have not always been aligned with political circumstances, focusing on new legislation and institutions while overlooking the enforcement dimension. Reform initiatives have also tended to overlook the interface between the public and the private sectors even though regulatory reforms have often been effective against corruption.

Activities at the Global Level

The Bank is expanding partnerships in a number of joint initiatives to strengthen governance. It is an active participant in promoting the OECD Convention on Combating Bribery of Foreign Public Officials (1997), the Forest Law Enforcement and Governance Ministerial Processes (from 2001), the Extractive Industries Transparency Initiative (2002), and the United Nations Convention against Corruption (2003). It works closely with several international anticorruption organizations and networks, including the Financial Action Task Force, the Partnership for Transparency Fund, the OECD Development Assistance Committee (DAC), and Transparency International. In fiscal 2007, the Bank collaborated with OECD-DAC Govnet to prepare an issues paper that sets out an agenda for engaging in global collective action to improve poor governance, for conducting joint corruption assessments, and for leveraging comparative strengths for a coordinated response to addressing corruption. (See **www.worldbank.org/governance** and **www.worldbank.org/integrity**.)

THE STRATEGY FOR MIDDLE-INCOME COUNTRIES

The 79 IBRD-eligible countries, most of them middle-income countries, are home to more than 70 percent of the world's population living on less than $2 a day. Improving assistance to these countries is thus critical to reducing poverty. For this reason, at its September 2006 Annual Meetings, the World Bank—with the encouragement of its shareholder governments—made a commitment to strengthening IBRD's effectiveness in partnering with middle-income countries to achieve better development outcomes and to collectively address regional and global concerns.

Middle-income countries have substantially improved the quality of their economic management in recent years. Access to market-based financing and risk-management tools has increased, and sovereign financing costs have declined to near all-time lows. But challenges remain. Capital market access remains concentrated in a few countries, and the cost of borrowing is typically much higher than that offered by multilateral development banks. Income inequality and large pockets of poverty persist, exacerbated by unevenness in access to education, physical infrastructure, and other public services. Many middle-income countries also face other persistent problems that cannot be solved in the short term. Solving these problems will require strengthening public institutions and improving the business environment and competitiveness of these countries.

Middle-income countries are repositories of extensive knowledge about and experience with development issues,

and they increasingly view themselves as partners, rather than as clients, of the Bank. Many promote development in other countries through foreign direct investment, bank lending, remittances, and even development assistance. Some contribute to IDA and may also partner in arrears clearance and debt-reduction exercises that benefit the world's poorest countries.

Some middle-income countries are also playing an increasingly important role in the governance of the global economy, helping develop the global agenda on issues such as trade and climate change. Some are delivering global public goods: combating infectious diseases, reducing greenhouse gas emissions, and preserving biodiversity.

Middle-income countries want the Bank to be more flexible and responsive; to offer a broader array of financing, risk-management, and credit-enhancement products; and to reduce turnaround times and transaction costs. Although lending and knowledge products have traditionally been offered together, these countries want more sharply focused and higher-quality knowledge services that are not tied to financing. They also want to make more extensive use of the Bank's convening capacity and experience in framing strategy and assembling portfolios of expertise and finance from multiple sources to help address collective issues.

To meet client countries' needs, the Development Committee strongly endorsed a new strategy crafted by the Bank that will improve performance in each of the Bank's three business lines: knowledge services, financial services, and strategy and coordination services.

In knowledge services, the Bank is seeking to leverage its research and expert services at the sectoral, country, and global levels through project cycle work, analytic work, training, institutional capacity building, technical assistance, and other advisory activities. It is also seeking to engage closely with national think tanks and other international organizations on knowledge exchange.

In financial services, the Bank is considering a full menu of financing and credit-enhancement and risk-management tools that can be offered to sovereign and nonsovereign entities.

In strategy and coordination services, the Bank will continue to offer its convening capacity and global reach to support country strategy work, including policy dialogue and delivery of expertise to promote growth and reduce poverty, and to address the provision of priority global and regional public goods. (See **www.worldbank.org/middleincomecountries**.)