

# Chairperson's Summary: Committee on Development Effectiveness (CODE)

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On May 7, 2008, the Committee considered *The World Bank Group Guarantee Instruments 1990–2007: An Independent Evaluation* and the draft management response. Comments by the external reviewers were circulated to the Committee as background information.

## Background

The Board of Executive Directors considered several management reports on the World Bank Group's (WBG) guarantee activities including reviews in 1997 and 2000 and technical briefings in 2005 and 2007. This Independent Evaluation Group (IEG) report is the first independent evaluation of the WBG guarantee instruments, undertaken at the request of the Board.

## IEG's Main Findings and Recommendations

The report assesses the effectiveness in the use of the WBG guarantee instruments and the delivery system of guarantee products within the WBG. The Director-General, Evaluations, highlighted three key findings from the report in his opening statement. First, guarantees have been effective in promoting key WBG strategic objectives, particularly in facilitating the flow of investment to high-risk sectors. Second, several weaknesses are evident in the political risk mitigation activities, including (1) competition among the WBG institutions that imposes additional transactional costs on clients and reputational risks to the WBG; (2) weaknesses in marketing; (3) supply-driven policies and restrictions placed by the mandates of WBG institutions; (4) limited staff awareness and skills, as well

as incentive issues in the World Bank and IFC with respect to guarantees; and (5) inconsistent pricing of the WBG political risk mitigation products. Third, the use of guarantee products of each WBG institution has fallen short of expectations because of these weaknesses.

The IEG report's main recommendation is for WBG senior management to "take a strategic approach and make a decision whether to maintain the existing organizational structure while addressing some of the important problems, or develop and propose an alternative organizational structure to the Board." The Director-General, Evaluations, highlighted this recommendation for the Board's attention and emphasized that maintaining the status quo, particularly in the delivery of political risk mitigation products, is not a tenable option and changes need to be made with or without organizational adjustment. The IEG report recommends that if a new organizational structure is proposed, management should consider at least three distinct perspectives: client, country, and product. Regardless of any organizational change, the IEG report recommended that WBG senior management take action to introduce greater flexibility in the use of guarantee

instruments in response to dynamic country and client needs and market developments.

### **Draft Management Response**

A joint Bank, International Finance Corporation (IFC), and Multilateral Investment Guarantee Agency (MIGA) response was presented, which noted that the IEG report provides analysis and recommendations that may be drawn on to enhance the effective use of WBG guarantees and insurance products. Management agreed with the general thrust of several IEG recommendations, such as the need to improve coordination and marketing. However, it noted that in attempting to synthesize the issues and recommendations, the report may have “oversynthesized” the findings at the WBG level, when most issues are not relevant across the board. Management also opined that a greater focus on the differences in mandates of MIGA, IFC, and the Bank (International Bank for Reconstruction and Development [IBRD] and International Development Association [IDA]) and on the WBG’s client-focused approach could have offered a different perspective to the IEG evaluation. In her opening statement, the MIGA Executive Vice President representing WBG management summarized the distinct mandates and clients served by each WBG institution. MIGA’s mandate is to foster development through the provision of political risk insurance for productive foreign investment and to mitigate risks for cross-border investments. IFC promotes private sector development, and its guarantees are used chiefly as unfunded loans to private investors. IBRD and IDA serve client governments, and these guarantees require sovereign counter-guarantees. The IBRD and IDA guarantees are more complicated instruments than the Bank’s loans, credits, or grants and are demanded mainly for complex projects in high-risk situations. Management emphasized that the WBG as a whole can bring a rich diversity of instruments, which should be used in a complementary fashion to support specific development objectives and client needs.

### **Overall Conclusions**

The Committee welcomed the timely discussion of the high quality and comprehensive IEG evaluation of the WBG guarantee instruments. There

was broad interest in this evaluation, and the need for more strategic thinking by senior management about the WBG approach to guarantee business in the longer term was emphasized. In this regard, there were diverse views on IEG’s recommendation for the WBG senior management to “make a decision whether to maintain the existing organizational structure while addressing some of the important problems, or develop and propose an alternative organizational structure to the Board.” The Committee remained neutral on the issue, neither recommending nor precluding organizational change, which is a long-term matter to be considered by management. Members stressed the need for a more in-depth analysis by management to determine the most appropriate way to address the market challenges and the weaknesses identified in the IEG report, and for the effective delivery and use of WBG guarantees.

Several speakers underlined that maintaining the status quo was not an option and suggested that the Management Response could be deepened to include a review of the three perspectives for organizational realignment suggested by IEG. On the other hand, some members noted the difficulties posed in organizational change, including impact on staff morale and legal implications. Regarding the possibility of amending the MIGA Convention, the Committee reiterated the understanding of the April 30 CODE meeting that it is looking forward to the management’s assessment of the constraints of the MIGA Convention before it could make any judgment on this issue.

Speakers stressed the importance of responding to market changes, being client oriented, and promoting the full array of WBG guarantee products. In this regard, they noted a need for a higher level of collaboration among the WBG institutions, improved marketing, greater staff awareness of the guarantee instruments, and appropriate staff incentives. Comments were also made on the overlap and competition of political risk products as raised by IEG and on the need to adjust and streamline internal policies and procedures, to consider the consistency of pricing policies across the WBG, and to think about a “single window” for guarantee products.

## Next Steps

The Committee supported the request made by some Executive Directors for a full Board discussion of this IEG report, together with the Management Response. The date of the Board discussion will be determined by the Corporate Secretariat after requisite consultation.

Management was asked to revise its response to the IEG report for the Board discussion, taking into consideration the comments raised at the meeting. A WBG legal opinion on the feasibility of a “single window” for guarantees, as well as any other legal questions that may arise during the forthcoming Board discussion related to the WBG delivery of guarantees, should be prepared in due course. The Committee Chairperson concluded that, in accordance with the approved IEG Disclosure Policy Statement, this evaluation report will be made publicly available following the Board discussion, unless the Executive Directors decide not to disclose.

The following main issues were raised at the meeting:

### **Organizational change**

Members considered the IEG report a good basis for considering longer-term improvements in the effective use of WBG guarantees in a changing market context, beyond the short- to medium-term focus of MIGA Operations Directions. In this context, IEG's main recommendation calling on the WBG senior management to decide whether to maintain or suggest changes to the existing organizational structure elicited a range of comments. Members and speakers noted the need for management to analyze and propose concrete solutions, including a timetable, to address the issues raised by IEG (for example, overlaps, competition, and pricing) and to streamline the delivery of WBG guarantees, increase competitiveness of guarantee products, and introduce more flexibility to adapt to client needs. Several speakers noted that the effective use and delivery of WBG guarantees may be enhanced to a certain extent through organizational adjustments within each WBG institution (for example, internal policy changes or updating the Operations Regulations

of MIGA) but also said that management should not rule out the option for organizational change. A few of them observed that changing the organizational structure will likely be even more difficult than amending the MIGA Convention and should be considered as a last resort.

Other speakers emphasized that maintaining the status quo is not an option and urged management to quickly review different alternatives. Likewise, they requested management to revise and deepen its response to the IEG report with more analysis on the issue of organizational change, including the three options suggested by IEG (for example, client, country, or product approach). A few of them also remarked that IEG could have been more specific in its recommendation for organizational change. A member questioned the appropriateness of the IEG recommendation and noted that it was not clear from the IEG report whether IEG found any fundamental deficiencies that could only be addressed through a change in organizational structure. In this regard, some members clarified that this IEG report should be considered a fact-finding paper as requested by the Executive Directors and that the idea of an organizational change for the WBG guarantee business had been actually raised by the management itself in past meetings. The negative impact on staff morale in raising the issue of organizational change was also noted by a few members.

*Management noted that multilateral development banks that have unified structures but no specialized guarantee institution do not have a larger share of guarantees in their product mix than the WBG, and the use of guarantees is not necessarily greater at these other multilateral development banks. Furthermore, none of the other multilateral development banks has had the same success in extending political risk insurance as MIGA. Accordingly, management was not recommending a restructuring of the organization but was focusing on strengthening WBG collaboration. At the same time, management welcomed a Board discussion on guarantees, underlining that the issue of changing the organizational structure required the involvement of the President, senior management of WBG, and*

*the Board. The MIGA General Counsel added that any changes in organizational structure will probably necessitate an amendment to the MIGA Convention. Such an amendment would require the affirmative vote of 60 percent of the Governors exercising 80 percent of the total voting power of the institution. Noting that the IEG report is expected to be disclosed, management commented on the need for a good communication strategy by the Board, particularly because the Committee discussions focused on organizational issues. It cautioned that the external public may have different views on the matter, which may affect the options available to management and the Board.*

*Management concurred that much could be done to strengthen the delivery of guarantees, which are part of a portfolio of services offered to clients. It committed to consulting senior management on how to deepen the Management Response. IEG reiterated that its evaluation findings indicate that substantial business opportunities are missed with the status quo, and so a more in-depth review discussion on the options for strengthening the delivery and use of guarantee products in a rapidly changing market situation were merited.*

### **Client-focused approach**

In considering the options for enhancing the effective use and delivery of WBG guarantees, several speakers urged WBG management to consider the client perspective option. They also encouraged WBG management to seriously consider the possibility of a “single window” for guarantees. A member stressed that the issue was not whether guarantee products were marginalized, but whether WBG clients’ need for different products (for example, loans, equity, guarantees) is being met. A speaker understood that if guarantees are underutilized, it also meant that clients are underserved. *In their opening statement, IEG staff clarified that its recommendations do not advocate that guarantee products should take precedence over various WBG instruments or propose a target level in use of WBG guarantee products.* Referring specifically to MIGA, another member expressed support for introducing

greater flexibility in its products by overcoming some of the constraints through the revision of its current Operational Regulations.

### **Cooperation within the WBG**

Several speakers stressed the need for greater collaboration among the three institutions based on their comparative advantages, and strengthening the coherence of the products offered, including their pricing. Some members echoed IEG’s remark that overlaps and competition did not necessarily imply redundancies, but required better WBG coordination. One speaker noted that there was sufficient external market competition and that competition within the WBG should be minimized. They and others called for more coordinated WBG efforts for marketing, increased staff knowledge of the guarantee products, and appropriate staff incentives.

A speaker urged management of IFC and the Bank to make better use of staff knowledge and skills available at MIGA. Regarding IFC’s readiness to work with MIGA and the Bank to market various political risk mitigation products, one member cautioned about the need for staff expertise in these products and the risk of conflict of interest. Another member suggested the possibility of placing MIGA under the umbrella of IFC, because IFC has a more extensive network for marketing and MIGA guarantees can complement IFC products. In this context, he also requested clarification about the issue of conflict of interest. Still another member cautioned against this idea. There was a question raised about the limited number of joint Country Assistance Strategies that included MIGA.

*Management agreed on the need for more WBG coordination. MIGA management noted that political risk insurance requires specialized skills, which are available in MIGA, but integration of MIGA work with IFC can lead to conflicts of interest, especially when there are claims that MIGA needs to mediate. The MIGA General Counsel noted that MIGA has a strict fiduciary duty embodied in its Convention that does not allow staff to take into consideration other interests outside the institution in the discharge of their duties.*

*The IFC Acting General Counsel pointed out that the overall objective of increased WBG coordination is probably less problematic from IFC's perspective, and the IFC Articles of Agreement (especially Article I, Purpose) are more flexible in the sense that they expressly recognize that IFC's role is to complement the activities of the Bank. Bank management briefly described how guar-*

*antees were incorporated into its outreach efforts to offer customized financial solutions focusing on IBRD countries, as well as training of both clients and Bank staff on the different financial products.*

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*Jiayi Zou, Chairperson*