

**REVIEW OF WORLD BANK CONDITIONALITY:
ISSUES NOTE**

**OPERATIONS POLICY AND COUNTRY SERVICES
WORLD BANK
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ABBREVIATIONS AND ACRONYMS

APL	Adaptable program loan
ARDE	Annual Review of Development Effectiveness
CAS	Country Assistance Strategy
CSO	Civil society organization
DFID	Department for International Development
DPL	Development policy loan
EIR	Extractive Industries Review
IBRD	International Bank for Reconstruction and Development
IDA	International Development Association
IMF	International Monetary Fund
LIC	Low-income country
LICUS	Low-income country under stress
MDG	Millennium Development Goal
MIC	Middle-income country
NGO	Nongovernmental organization
OED	Operations Evaluation Department
OPCS	Operations Policy and Country Services
PRS	Poverty reduction strategy
PRSP	Poverty Reduction Strategy Paper
PSIA	Poverty and Social Impact Analysis
SAPRI	Structural Adjustment Participatory Review Initiative
SWAp	Sectorwide approach

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I. BACKGROUND

1. Conditionality has been a subject of debate ever since policy-based lending became an important instrument of World Bank financial support in the early 1980s, and its practice has come under renewed scrutiny in recent years. Reviews of the effectiveness of development assistance over the past decades have demonstrated that reforms are more likely to be sustained when the reform program emerges from a country's own domestic political process and is suited to that country's specific circumstances. The practice of conditionality itself has evolved over time, as the development community recognizes the limits of generally applicable development models in dealing with the complexity of supporting policy reforms in countries that have different circumstances and varying levels of constancy and commitment. The past few years have seen the emergence of new approaches to policy-based lending and increased efforts by the IMF and the World Bank to analyze and improve the effectiveness of their support for policy reforms. As multilateral and bilateral donors have shifted some of their development aid in low-income countries (LICs) to budget support, they are now faced with the practical questions of the appropriate type and nature of the conditions attached to their support for recipient countries' development programs.

2. ***Conditionality Review.*** The Bank's approach to conditionality has evolved substantially since the 1980s. The conditionality review is intended to document this evolution, take stock of the lessons of experience, and take a fresh look at the Bank's practice of conditionality. It will use the considerable body of existing research, as well as new analysis, to review how these lessons have been reflected in recent trends and approaches.

3. ***Outline of the Conditionality Review.*** The review, to be carried out during FY05, will consist of a broad work program that involves several workshops and discussions with Executive Directors, governments, donors, development practitioners, civil society organizations, and other parties interested in contributing to the debate. A series of issues notes, research papers, and good practice notes will be prepared to address different aspects of the experience and practice of conditionality; it is expected that one outcome of the review will be a set of good practice principles for Bank support of policy-based programs. This effort will form the basis of the Bank's response to the Development Committee's request that the Bank "review its own policy and practice on conditionality" and "report on the continued efforts by the Bank and the Fund to streamline their aggregate conditionality" by the Fall 2005 meeting.¹ This review coincides with the IMF's review of its own conditionality, which is expected to be discussed by the IMF's

¹ See *Development Committee Communiqué*, Joint Ministerial Committee of the Boards of Governors of the Bank and the Fund on the Transfer of Real Resources to Developing Countries, October 2, 2004, para 7.

Board by February 2005 and International Monetary and Financial Committee at the Spring Meetings.

4. ***Outline of the Issues Paper.*** This issues note identifies the key questions to be addressed in the review and sketches its proposed elements.² Section II defines what is meant by conditionality for the purposes of this review. Section III notes some of the existing analytic work on conditionality that this review will draw on, and Section IV mentions some of the recent trends in the World Bank's approach that will be important for the review. Section V suggests set of possible key issues for the review, and Section VI provides a tentative outline of key principles that might guide the future use of conditionality. Section VII concludes with a preliminary work plan for the review.

II. CONDITIONALITY: WHY AND WHEN?

5. International aid agencies (donors) typically allocate their aid resources with the expectation that the recipient country will use them in a way that is consistent with a set of objectives previously agreed between both parties. For the most part, such objectives relate to actions that are expected to improve the economic and social development of the recipient country.³ The actions may be in the form of a project that involves specific physical activities (such as building a school) and the expenditures needed to undertake these activities; or they may be in the form of commitments on specific development policies. Conditionality is involved whenever the donor has the right to halt the flow of resources if the recipient country does not meet certain conditions.

6. ***Rationale for Conditionality.*** All donors use conditionality in one form or another. Whether they do so implicitly or as part of an explicit binding agreement, they share a similar reasoning for the use of conditionality: to ensure that the assistance actually contributes to the country's development objectives (development effectiveness rationale), and to ensure that the resources are used for the purposes intended, (fiduciary rationale). Like other international aid agencies, the Bank uses conditionality to provide assurances that the resources it provides are used both effectively and responsibly. The Bank must be guided in all of its decisions by the purposes of the institution set out in its Articles of Agreement: to support its member governments in their efforts to further their development and reduce poverty. The Bank's due diligence on development effectiveness and fiduciary responsibilities is mandated by the requirement to "make arrangements to ensure that the proceeds of any loan are used only for the purposes for which the loan was granted, with due attention to considerations of economy and efficiency and without regard to political or other noneconomic influences or considerations" (IBRD, Article III,

² This issues paper is part of the FY05 World Bank Review of Conditionality. For questions and comments, contact Stefan Koeberle (skoeberle@worldbank.org) or Jaime Jaramillo-Vallejo (jjaramillo1@worldbank.org), Country Economics, Operations Policy and Country Services (OPCS), World Bank.

³ At the level of bilateral agencies, development may be understood in political terms. As a rule, multilateral development agencies are explicitly banned from interfering in political affairs, and they use only economic or social considerations in their decisions.

Section 5). Such considerations apply equally to IDA, the World Bank's concessional financing window for low-income countries.⁴

7. ***World Bank Application.*** The World Bank applies these development effectiveness and fiduciary considerations in each of its borrowing countries when deciding on its strategy for the country, including the overall envelope for financial assistance. At the operational level, the Bank takes these considerations into account as it delivers resources to each country.⁵ The Bank carries out its due diligence through several vehicles.

- The *Country Assistance Strategy* (CAS) provides the Bank's strategic business framework for supporting a country's development. To effectively calibrate the Bank's support, the CAS typically uses triggers and performance indicators for different scenarios that modulate the Bank's assistance within a defined lending envelope, and that indicate a mix of lending instruments.
- IDA donors mandate that country performance play a large role in the *allocation of IDA resources*. This approach is based on the understanding that aid is most effective in countries with good policy environments. An annual exercise provides nominal allocation of IDA resources among countries on the basis of their incidence of poverty and their policy environments.⁶
- *Analytic and advisory services* are the main vehicles for the Bank's policy dialogue with governments. The largest category of analytic services is economic and sector reports, which include diagnostic reports on the strength and weaknesses of the country's fiduciary arrangements, as well as poverty assessments and environmental analyses. Analytic and advisory services also include policy notes, workshops, and ad hoc advice with which the Bank helps the country develop and consider policy options and shares international lessons of experience.
- The Bank's *operational policies*, which are approved by its Board of Executive Directors, involve explicit requirements for project and program design and implementation.⁷
- *Development policy lending* is the Bank's main instrument for providing rapidly disbursing policy-based financing to support a country's program of

⁴ See IBRD Article (of Agreement) III, Section 5; and IDA Article (of Agreement) V, Section 1. Similarly, Article I of the IBRD Articles of Agreement also states "that the more useful and urgent projects, large and small alike, will be dealt with first."

⁵ When making these allocative decisions, the Bank also takes into account such factors as the country's credit worthiness.

⁶ On the allocation of IDA resources, see *Allocating IDA Funds Based on Performance: Fourth Annual Report on IDA's Country Assessment and Allocation Process*, 2003.

⁷ Of particular importance to borrowers are the World Bank's 10 safeguard policies: environmental assessment, natural habitat, pest management, involuntary resettlement, indigenous peoples, forestry, safety of dams, cultural property, projects on international waterways, and projects in disputed areas.

policy and institutional actions. OP/BP8.60 sets out the requirements for development policy lending, including the need for an adequate macroeconomic policy framework. The Bank is responsible and accountable for assessing the adequacy of a country's macroeconomic policy framework, taking into consideration issues that the IMF may have.⁸

- When the Bank finances *investment projects*, it agrees on a series of undertakings that typically include requirements regarding the purchase of goods and services, which are designed to ensure that the proceeds are used for the purposes intended. While the Bank has increasingly discouraged the use of conditionality in investment lending,⁹ investment projects may sometimes include agreements on particular policy undertakings that are important for achieving the project objectives. In particular, sectorwide approaches (SWAs) and adaptable program loans (APLs) may involve an understanding between the Bank and the recipient government on a sectoral development program. While such cases are outside the purview of this review, some of its conclusions and principles may be broadly applicable to them.

8. ***Defining World Bank Conditionality.*** This exercise of due diligence implies a set of requirements and preconditions that the recipient country is expected to meet in order to receive financial assistance. However, it is important to distinguish this from the specific conditions attached to the Bank's lending. This review will focus on the conditionality associated with the World Bank's policy-based lending.¹⁰ More precisely, in the Bank context, conditionality denotes the set of explicit conditions upon which the Bank disburses under development policy lending, and which are listed as legal conditions in the Bank's Loan Agreements. Conditionality thus includes all the specific conditions for multitranches operations, and the prior actions for programmatic operations.¹¹

9. ***Distinguishing What Is Not Conditionality.*** Some loans have conditions of Board presentation, but these are not part of conditionality: they are not included in the legal agreement and are not legally binding; rather, they are requirements imposed by management, and they may be waived before a Loan Agreement is signed. In addition, many of the ingredients included in a typical policy matrix for a policy-based loan (such as benchmarks, outcomes, expected results, and progress indicators) are not conditionality. They are indicative understandings on policy actions that a country

⁸ The experience of collaboration between the Bank and the IMF is the subject of regular reviews. The next review on Bank-Fund collaboration is scheduled to take place before the end of 2007.

⁹ See the staff guidance note *Disciplined Use of Conditionality in Lending Operations* issued by OPCS on September 13, 2004.

¹⁰ Policy-based lending is used here to denote financial support in the form of loans or grants given by the World Bank in the form of the now-retired adjustment lending (under OD 8.60) and development policy lending (since the introduction of OP/BP 8.60 in September 2004).

¹¹ Programmatic operations involve a medium-term framework for a series of typically single-tranche operations that are based on completed actions.

intends to undertake. They are used as a reference framework and management tool, but nonperformance does not result in suspension of disbursement or other explicit sanctions. Programmatic operations use triggers that are flexible reference points to inform the Bank's decision to proceed with the next operation, and that are thus clearly distinguishable from the binding conditions of traditional tranching operations. This review will provide an opportunity to discuss how the evolution of all these different components of the Bank's policy-based lending have contributed to a departure from the traditional conditionality of the 1980s.

III. PREVIOUS REVIEWS OF CONDITIONALITY

10. Conditionality in policy-based lending has been the subject of extensive research for more than two decades. This review will build on some of the work carried out by the Bank itself, experiences of other international financial institutions, academic literature, and analysis by civil society organizations.

A. Formal Reviews of Conditionality Undertaken by the Bank

11. The Bank has been analyzing its conditionality since the introduction of policy-based lending in the early 1980s. These efforts include the following:

- ***Early reviews of conditionality*** The Bank reviewed its experience with conditionality on in three very detailed reports on adjustment lending in 1986, 1990, and 1992.¹² In addition, in 1995 the Operations Evaluation Department (OED) conducted an extensive study of the Bank's experience with adjustment lending in the 1980s, including conditionality.¹³
- ***World Bank reviews of conditionality in the 1990s.*** The Bank's reviews of conditionality in the 1990s focused more on the effectiveness of its lending instruments used in policy-based lending, and less on the specific design of programs and the associated conditions. These reviews were extensively discussed by the Executive Directors and widely shared with external audiences, particularly as a preparation for the update of the Bank's operational policy on adjustment lending.
- ***Research on aid effectiveness.*** In the 1990s the Bank's research focused on aid effectiveness, trying to distill lessons from the institution's own experience.¹⁴ A dominant lesson from that body of research is the importance

¹² See *Structural Adjustment Lending: A First Review of Experience*, Operations Evaluation Report No. 6409, World Bank, September 24, 1986; *Report on Adjustment Lending: Policies for the Recovery of Growth* (R90-51, IDA/R90-49), March 26, 1990; and *The Third Report on Adjustment Lending: Private and Public Resources for Growth* (R92-47, IDA/R92-29), March 24, 1992.

¹³ C. Jayarajah, and W. Branson, *Structural and Sectoral Adjustment, World Bank Experience, 1980-92*, Operations Evaluation Department, 1995.

¹⁴ See, for example, D. Dollar, and L. Pritchett, *Assessing Aid: What Works, What Doesn't, and Why*, World Bank Policy Report, 1998; D. Dollar, and J. Svensson, *What Explains the Success or Failure of*

of a country's ownership of its reform program: donors can advise on and support, but cannot buy or induce, economic reforms. Thus government willingness to reform—where possible, with broad popular support—is essential to successful programs. One conclusion could be to forgo ex ante conditionality involving promises of future actions and instead allocate policy-based loans on the basis of a country's track record. Research on aid effectiveness also suggests that programs yield long-term benefits if a country's policy environment is favorable. Indeed, research identified a clear and significant positive relationship between country policy and institutional characteristics on the one hand, and adjustment loan success rates on the other. This suggests that policy-based lending should focus on countries with good policies and high overall poverty rates or high incidences of poverty in specific regions. Empirical studies emphasize that policy changes are driven primarily by the domestic political economy, not by foreign assistance or policy-based lending.¹⁵ More recent contributions confirm the relevance of ownership as the driver of reforms, by showing that surges in finance do not lead policy reforms.¹⁶

- ***Annual Review of Development Effectiveness (ARDE) 1999.*** As OED's annual report to the Executive Board, the 1999 ARDE gave special attention to the relationships among ownership, conditionality, and participation.¹⁷ The report included a discussion of the tension between ownership and conditionality, the need to manage for results, and the issue of partnership and strategic selectivity. It noted that conditionality could foster a country's commitment to ongoing reform when there was true ownership of those policies.¹⁸ Moreover, when there was ownership, conditionality allowed the borrowing country and the Bank to develop and nurture mutual trust and commitment. The report suggests a new and flexible approach, with conditionality as a mutual commitment device between the Bank and the borrower, suitably combined with capacity building to level the playing field for the country and its development partners. Participation by development partners, both domestic and external, was seen as essential to buttress ownership and to reduce the risks of coercive conditionality that could come out of negotiations between a hard-pressed country and powerful lenders.

Structural Adjustment Programs? World Bank Development Research Group, 1998; and S Devarajan, D. Dollar, and T. Holmgren, *Aid and Reform in Africa*, World Bank Paper, 2001.

¹⁵ S. Devarajan, D. Dollar, and T. Holmgren, *Aid and Reform in Africa—Lessons from Ten Case Studies*, World Bank Development Research Group, December 1999.

¹⁶ A. Alesina, and D. Dollar, *Who Gives Foreign Aid to Whom and Why?* NBER Working Paper 6612, National Bureau for Economic Research, Cambridge, Massachusetts, 1998.

¹⁷ *World Bank, Annual Review of Development Effectiveness—Toward a Comprehensive Development Strategy*, Operations Evaluation Department, Report 19905, November 19, 1999.

¹⁸ As a framework for assessing borrower ownership, the OED report refers to John Johnson and Sulaiman Wasty, *Borrower Ownership of Adjustment Programs and the Political Economy of Reform*, World Bank Discussion Paper No.4 (Washington DC, World Bank, 1986).

- ***Adjustment Lending Retrospective.*** One objective of the Adjustment Lending Retrospective of June 2001 was to lay the groundwork for a review of the Bank's approach to policy-based lending, paving the way for a revision of the relevant operational policies.¹⁹ The Retrospective took stock of the major trends and developments of two decades of adjustment lending, concluding that adjustment lending's initial focus on short-term balance of payment support had largely given way to a focus on sustained support for complex and often unpredictable medium-term reforms. It suggested that a programmatic approach was better suited to deal with the need to support countries in their increasing focus on medium-term structural and institutional policy programs, and that monitoring and evaluation were as important for success as due preparation of the operation. The Retrospective indicated that conditionality cannot be a substitute for country ownership and reform readiness. It acknowledged that the extent of country ownership is not easy to determine in practice, discussed the limitations of conceptual frameworks for assessing ownership, and suggested that a country's track record is typically one of the more robust indicators of commitment. It also pointed out that conditionality through a programmatic approach allows the Bank to base its support on performance rather than on promises.

12. ***Recent World Bank Reviews of Conditionality.*** Much of the Bank's operational work on policy-based lending in the past few years has focused on the practice of conditionality. In these reviews the Bank has paid significant attention to the different design aspects of conditionality, including those associated with the initiatives to enhance country ownership of programs and streamline conditionality as well as with Bank-Fund collaboration.²⁰

- ***Programmatic Adjustment Lending Retrospective.*** The Programmatic Adjustment Lending Retrospective of July 2003²¹ took stock of experience with the programmatic approach, with the intention of identifying best practices and determining whether this approach had lived up to its promises. Its main conclusion was that the programmatic approach had been robust and effective in a wide range of country circumstances. Early experience with the approach was positive largely because of the design features that provided sufficient flexibility to facilitate a stronger focus on results, participation, and harmonization. Reliance on prior actions and on subsequent flexible triggers was seen as key to allowing greater ownership by the borrowers and to enhancing the predictability of Bank support. The Retrospective also highlighted the relevance of assessing beforehand both the poverty links and the fiduciary concerns of the program.

¹⁹ *Adjustment Lending Retrospective*, Report 22723, World Bank, June 15, 2001.

²⁰ See J. E. Stiglitz, *Towards a New Paradigm for Development*, 1998 Prebisch Lecture at UNCTAD, 1998, and J. D. Wolfensohn, *A Proposal for a Comprehensive Development Framework*, Speech, 1999. See also, H. Köhler, *Streamlining Structural Conditionality*, IMF, 2000.

²¹ *Programmatic Adjustment Lending Retrospective*, Report 26315, World Bank, July 11, 2003.

- **Reviews of Bank-Fund collaboration** The Bank’s review of its conditionality has also been carried out in the context of reviews on Bank-Fund collaboration, which were discussed by the Boards of both institutions.²² Building on the earlier division of labor set out in the Concordat of 1989, a strengthened framework for Bank-Fund collaboration was introduced in 2001. Under this framework, staff of both institutions are expected to provide coherent support to countries through early and systematic coordination on programs and conditionality, with each institution focusing its conditionality on those areas that are deemed critical for the success of their respective programs. A special framework is provided for LICs, where the Poverty Reduction Strategy Paper (PRSP) process defines an overarching framework for that collaboration. The reviews carried out thus far show that both institutions have made reasonably good progress in the strengthened collaboration framework, but that there is room for improvement as well as a need to monitor and review developments in the future.²³ The next review of Bank-Fund collaboration is expected to be concluded by the end of 2007.
- **Annual Review of Development Effectiveness 2003.** The 2003 ARDE focused on the effectiveness of Bank support for policy reform, acknowledging that the Bank’s approach is grounded in the country’s leadership and ownership of the development agenda, with the support customized to country circumstances.²⁴ The ARDE noted that most countries had improved their development policies, and that those improvements had translated into higher growth rates for their economies. Bank lending was concentrated in countries that had relatively good policy environments, where the support backed further improvements in policies within a stable reform environment. The review noted, however, that the Bank’s conditionality had not resulted in good outcomes in situations of high uncertainty. Strong analytic underpinnings were identified as a major factor contributing to the success of policy programs. Nevertheless, the review noted that the Bank had not always paid sufficient attention to alternative perspectives or to individual country circumstances; it said that generic “best practices” should give way to intensified efforts to customize and adapt knowledge to specific localized problems, taking country experience into account. The review called for the Bank to “experiment with approaches that would complement intermediate indicators and conditions with indicators of direct poverty reduction results or

²² See *Strengthening IMF-World Bank Collaboration on Country Programs and Conditionality* (World Bank SecM2001-0461/1 and IMF SM/01/219), August 24 and 23, 2001, respectively; *Strengthening IMF-World Bank Collaboration on Country Programs and Conditionality—Progress Report* (World Bank SecM2002-443 and IMF SM/02/271), August 2002; and *Strengthening IMF-World Bank Collaboration on Country Programs and Conditionality—[Second] Progress Report* (World Bank SecM2004-0070 and IMF SM/04/57), February 24, 2004.

²³ The reviews have been based on surveys of authorities, Executive Directors, mission chiefs in the IMF, and country directors in the Bank, complemented with desk reviews of case studies and analytic work.

²⁴ *2003 Annual Review of Development Effectiveness—The Effectiveness of Bank Support for Policy Reform*, Operations Evaluation Department, World Bank, 2004.

other outcome-related indicators.” It also encouraged the Bank to find ways to diffuse the tension between its instruments of support and the efforts to promote country-led partnership approaches to development.

- **Board briefings.** As the World Bank’s Board considers individual operations and operational policies, Executive Directors regularly use these opportunities to make statements on the general lessons they draw on the practice of conditionality. In particular, the Board discussed these issues in the context of the Board papers on Bank-Fund conditionality and adjustment lending, and OED reports, mentioned above. Beyond that, Executive Directors have been briefed regularly on the evolution of the Bank’s lending.
- **Workshops on conditionality** Over the past few years, the Bank has held a number of formal seminars on the experience with conditionality, for some of which Bank prepared analytic papers. In early July 2004, the Bank convened an international seminar in Paris to look into the role and effectiveness of conditionality in lending programs, bringing together the IMF, other multilateral development banks, bilateral donors, borrowing countries, civil society organizations, and think-tanks.²⁵ Participants in the seminar generally acknowledged that the traditional understanding of conditionality as leverage was a thing of the past. The experience of the 1980s and 1990s suggests that conditionality is not necessary if there is true country ownership, and that it is not likely to be effective in the absence of ownership. Instead, conditionality should be thought of as part of a cycle that also includes policy dialogue and capacity building, with the participation of key stakeholders. Most participants also acknowledged that policy advice cannot be prescriptive or based on standardized development models, but should help countries develop their own solutions for applying principles that have been recognized as valid development objectives—such as the rule of law, transparency, fiscal sustainability, and efficient service delivery. The use of budget support for low-income countries called for aid agencies to continue their efforts at harmonizing their policies and procedures and increasing the predictability of their support. Participants raised questions about the greater reliance on process conditionality, and recognized that fragile states present a completely different set of challenges.

B. Recent External Work on Conditionality

13. Examination of the Bank’s experience with conditionality has included external consultations with civil society and other stakeholders. The two most important consultative reviews are the Structural Adjustment Participatory Review Initiative (SAPRI) concluded in 2001, and the Extractive Industries Review (EIR) concluded in 2004. These two consultations, which were directed by prominent figures from outside

²⁵ A transcript of the proceedings and papers prepared for the seminar are available on the World Bank’s website at [www.worldbank.org/ projects and programs/consultations/review of World Bank conditionality](http://www.worldbank.org/projects_and_programs/consultations/review_of_World_Bank_conditionality).

the Bank, concluded with reports and discussions between the representatives of participating civil society and the Bank.²⁶ The results of these consultations were reflected in the recent change in practice and operational policy.²⁷

14. **External Critiques of World Bank Conditionality.** Conditionality has been the subject of extensive critiques from different political directions. The Meltzer commission on international financial institutions advocated limiting policy-based lending to countries with good policies.²⁸ Some civil society organizations have taken aim at what they consider to be excessive intrusiveness and lack of transparency in the Bank's policy-based lending. They also criticize the Bank's advice for being too narrow, and policy-based lending for insufficiently considering policy alternatives in specific areas.²⁹

15. **Academic Literature.** Conditionality has been something of a hot topic in the academic literature. Research has been commissioned by groups of borrowing countries, such as the Group of 24,³⁰ bilateral donors have reviewed their own positions on conditionality,³¹ and think-tanks have reacted to calls from civil society and other stakeholders.³² Other recent research looks at World Bank conditionality, selectivity,

²⁶ For SAPRI, see <http://www.worldbank.org/research/sapri/index.htm> for EIR, see <http://www2.ifc.org/ogmc/>.

²⁷ *From Adjustment Lending to Development Policy Lending*, OPCS, World Bank, 2004

²⁸ A. Meltzer, C.F. Bergsten, C. W. Calomiris, T. Campbell, E.J. Feulner, W.L. Hoskins, R.L. Huber, M. H. Johnson, J.I. Levinson, J.D. Sachs, and E.E. Torres., *Results and Recommendations of the International Financial Institution Advisory Commission, Final Report to the U.S. Congress and Department of Treasury*. Washington, D.C., 2000.

²⁹ *Money Talks: How Aid Conditionality Continues to Drive Utility Privatization in Poor Countries*, Action Aid, 2004; *Streamlining of Structural Conditionality—What Has Happened?* Eurodad, May 2003; *From 'Donorship' to Ownership? Moving Towards PRSP Round Two*, Oxfam, 2004; *Economic Policy Conditionalities*, Save The Children, 2004; and *Zambia: Condemned to Debt: How the IMF and the World Bank Have Undermined Development*, World Development Movement, 2004.

³⁰ The Group of 24 discussion papers include: A. Buirra, *An Analysis of IMF Conditionality*, June 2002; R. Kanbur, *IFIs and IPGs: Operational Implications for the World Bank*, June 2002; D. Kapur, *A Critique of G-7 Proposal on Reforming the MDBs*, April 2002; R. Wade, *The U.S. Role in the Malaise at the World Bank: "Get Up, Gulliver!"* September 2001; Y. C. Park, and Y. Wang, *Reform of the International Financial Systems and Institutions in Light of the Asian Financial Crisis*, July 2001; J. A. Ocampo, *Recasting the International Financial Agenda*, July 2001; K.S. Jomo, *Growth After the Asian Crisis: What Remains of the "East Asian Model?"* March 2001; D. Cohen, *The HIPC Initiative: How Really Good Is It?* July 2000; R. Webb, *Governance-Related Conditionalities of the IFIs*, July 2000; and A. Oyejide, *Interests and Options of Developing and Least-Developed Countries in a New Round of Multilateral Trade Negotiations*, May 2000.

³¹ *Partnerships for Poverty Reduction: Changing Aid Conditionality*, Department for International Development (DFID), London, September 2004 and *Post-Washington Consensus: A Few Thoughts*, Discourse Discussion paper 004/2004, Bundesministerium fuer wirtschaftliche Zusammenarbeit (BMZ), Berlin, May 2004.

³² For example, P. Collier, and D. Dollar, "Development Effectiveness: What Have We Learnt?" *Economic Journal*, 114 (June), F244-F271; P. Mosley, J. Hudson, and A. Verschoor, "Aid, Poverty Reduction and the 'New Conditionality,'" *Economic Journal*, 114 (June), F217-F243; P. Mosley, F. Noorbakhsh, and A. Paloni, "Compliance with World Bank Conditionality: Implications for the Selectivity Approach to Policy-Based Lending and the Design of Conditionality," *Credit Nottingham* No.03/20; and M. Khan, and S. Sharma, 2003, "On IMF Conditionality and Country Ownership," *World Bank Research Observer*, vol. 18, n2: 227-248.

performance-based conditionality, and the implications of the aid effectiveness research.³³ The conditionality review will closely look at the main conclusions and operational lessons emerging from this extensive body of academic literature.

IV. RECENT TRENDS AND APPROACHES IN WORLD BANK CONDITIONALITY

16. This review of conditionality is taking place against the background of several important changes that have taken place in recent years. In the first place, the Bank's approach and practice have broadly moved away from traditional conditionality, which focused on short-term macroeconomic adjustment and removing major economic distortions. The research on aid effectiveness suggested that the problem with much of conditionality in the past was that it did not help promote policy reform—either because it was too coercive (when governments undertook the reforms without a domestic political consensus, only to reverse them subsequently) or was not credible (when governments knew that donors would provide the funding in any case, even when reforms were not implemented).³⁴ Important trends that reflect this departure from the traditional approach include the notion of support to country programs, the efforts to streamline conditionality, the emergence of programmatic lending, and the adoption of new operational guidelines for policy-based lending.

17. *Supporting Country Programs.* The practice of conditionality has evolved from the idea that governments must meet a set of conditions to receive Bank financing, to an approach in which the Bank supports policy reform in client countries. The Bank has learned from experience that attempting to apply more conditions in the hope of achieving at least a partial compliance is of limited effectiveness, particularly in entrenched poor performers. The review of conditionality will provide an opportunity to sketch the path the Bank has traveled—and still has to go—in answering the question “How can we best support countries in their development of policies and institutions?”³⁵ Development practitioners may be reaching a consensus on some of the answers: first, by helping the countries undertake the analytic work to design and implement country-tailored policies; second, by carefully assessing when a country's commitment to a policy program and institutional capacity provide the preconditions for effective implementation; and third, by ensuring that the country broadly “owns” the policy

³³ Recent papers include C. Adam, and J. Gunning, “Performance-Based Conditionality: A European Perspective,” *World Development* Vol. 32, No. 6, pp. 1059-1070, 2004; Bulir and Hamann, “Aid Volatility, an Empirical Assessment,” *IMF Staff Papers*, Vol. 50 No. 1 (2003); O. Morrissey, “Conditionality and Aid Effectiveness Re-evaluated,” *World Economy*, February 2004; T. Killick, “Aid and the Political Economy of Policy Change,” *Routledge and Overseas Development Institute* (1998); T. Killick, “Politics, Evidence and the New Agenda,” *Development Policy Review* 22(1), pp 5-29 (2004); S. Koeberle, “Should Policy-Based Lending Still Involve Conditionality?” *World Bank Research Observer*, vol.18, no. 2 (Fall 2003), pp.249-273; A. Winters, N. McCulloch, and A. McKay, “Trade Liberalization and Poverty: The Evidence So Far,” *Journal of Economic Literature*, Vol. 42, No. 1 (2004).

³⁴ Examples include three structural adjustment loans in a row to Kenya for the same agricultural price reform.

³⁵ By contrast, using policy-based lending to “buy reform” has never been a permissible purpose for the World Bank, as the General Counsel discussed in an early legal opinion. (Vice President and General Counsel, “Authorized Purposes of Loans Made or Guaranteed by the Bank,” April 1988, para 17).

program. And finally, in some cases, even when client “owns” the contours of the policy program, members of the government might find it useful to have a few specific actions as part of the triggers or conditions for a Bank loan. In this case, the use of conditionality may help the client country promote policy adoption and implementation.

18. ***Streamlining Conditionality.*** Frequently the debate on conditionality has tended to focus narrowly on the average number of conditions per loan, which has usually been perceived as excessive relative to the government’s implementation capacity. In practice, this issue is more complex: the number of conditions says little about the relevance and usefulness of those conditions. In some cases a greater level of detail may even be desirable, when a more specific roadmap is needed to operationalize the policy program; and the trend toward multisector operations and donor harmonization also goes hand in hand with a broader coverage. Nonetheless, over the past few years, the average number of conditions in World Bank policy-based loans has been substantially reduced. Recent Management instructions and guidelines to staff have reiterated the importance of limiting the number of conditions.³⁶ The average number of conditions³⁷ fell from above 35 in the late 1980s to about 15 in FY04 (see Figure 1), except in FY92-93, when the average number of conditions was over 40. If indicative benchmarks are included,³⁸ the total number has fallen from around 60 to 39 during the same time. While the average number of conditions has tended to decrease across all Bank lending, the number of conditions for IBRD countries has tended to be slightly higher than for IDA countries (see Figure 2).³⁹

19. ***Emergence of Programmatic Lending.*** Over the past few years, the Bank has increasingly used a programmatic approach for its policy-based lending.⁴⁰ This approach involves a series of single-tranche operations that are sequentially presented to the Bank’s Board of Executive Directors, with a medium-term framework specified at the outset—including completed prior actions, monitorable progress indicators, and expected prior actions (triggers) for subsequent operations. To the extent possible, programmatic approaches align disbursements with the borrowing country’s annual budget cycle. By building on completed actions, instead of promises of future actions, a programmatic approach contributes to systematic policy implementation. Programmatic lending is usually used to support complex medium-term institutional reforms. Poverty reduction

³⁶ Staff guidance note *Disciplined Use of Conditionality in Lending Operations* issued by OPCS on September 13, 2004, and *Good Practice Note for Designing Development Policy Operations*, World Bank, OPCS, October 2004.

³⁷ This is based on policy conditionality, including prior actions preceding Board presentation, effectiveness conditions, and conditions for tranche release, which are set out in the legal agreements signed by the borrowing government and the World Bank.

³⁸ Indicative benchmarks are covered in the program documentation but are not explicitly identified as prior actions or tranche release conditions.

³⁹ The average for IBRD countries reflects the high number of conditions associated with two complex adjustment loans in crisis situations that were subject to extensive discussions by the Executive Directors: the Argentina Economic Recovery Support Structural Adjustment Loan (31 conditions) and the Turkey III Programmatic Financial and Public Sector Structural Adjustment Loan (35 conditions). When these two loans are excluded, the average declined from 18.9 to 15.2 conditions.

⁴⁰ *Programmatic Adjustment Lending Retrospective*, Report 26315, July 11, 2003.

support credits (PRSCs) are emerging as a vehicle that incorporates these principles, basing social and structural reforms in IDA countries on the poverty reduction strategies articulated in each country's PRSP.

Figure 1. Average Number of Conditions and Desired Actions per WB Adjustment Loan/Credit, FY80-04 Agreement, FY95-04

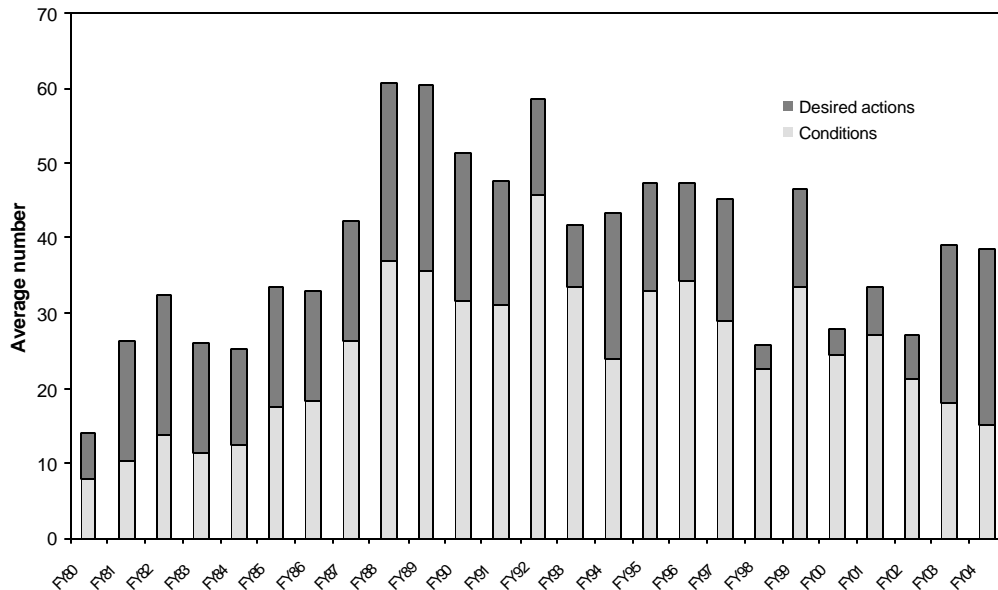
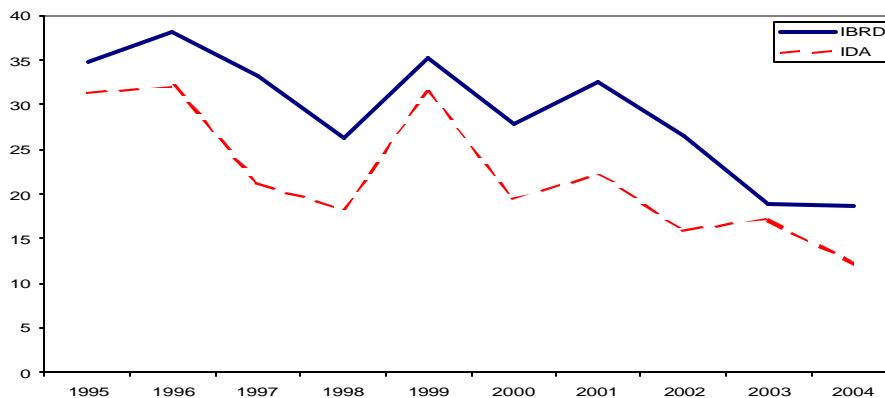


Figure 2. Average Number of Legally Binding Conditions by Agreement, FY95-04



20. ***From Adjustment Lending to Development Policy Lending: Update of World Bank Policy.*** In August 2004, the Bank formally recognized the significant changes that had taken place in its policy-based lending by issuing a new operational policy statement for use by Bank staff. The policy change—which replaced adjustment lending with

development policy lending⁴¹—was the result of extensive discussions over two years with Executive Directors and consultations with a wide variety of stakeholders, including governments, civil society organizations, private sector representatives, and academics. In replacing the previous guidelines, the Bank retired prescriptive passages on specific policy areas such as privatization, financial sector reform, and public sector reform. The new development policy lending explicitly aims at supporting a country’s program of policy and institutional actions to promote growth and achieve sustainable reductions in poverty. These programs are expected to be based on country and sectorwide analytic work (carried out by the countrywide itself, third parties, or the Bank) that covers the country’s fiduciary arrangements; its environment, including forests and other natural resources; and the likely poverty and social impacts of key policies supported by the operation. As regards conditionality, the new policy mandates that conditions should be confined to those actions that are critical for implementing the country’s program to achieve the expected results. Programs under the new policy are expected to reflect policies that have been developed in consultation with stakeholders in the country, and to include a results framework that allows adequate monitoring and evaluation.

21. ***Emerging Good Practice.*** The last few years have also seen the emergence of good practices in the Bank’s application of conditionality.⁴² Drawing on the lessons learned from over two decades of experience with policy-based lending, well-prepared operations to a large extent already reflect such good practices.

- ***Ownership.*** It is, good practice to base development policy lending on an assessment of the overall adequacy of the country’s own development strategies, its commitment, and its readiness for reform. Given the complexity of country situations, such an assessment should go beyond a simplistic and unequivocal concept of ownership that presupposes a uniform government position or a full consensus. A realistic assessment acknowledges that reforms may be owned by some constituencies and opposed by others who stand to lose from them. Instead, a careful identification of stakeholders and assessment of the country’s political economy—informed by poverty and social impact analysis where appropriate—may help in identifying the scope for a sustainable reform program.
- ***Criticality.*** Experience also shows that the quality and impact of policy-based lending are better with a limited set of conditions that are focused on the critical actions needed to achieve key outcomes, and that include the necessary institutional arrangements for monitoring and evaluating their results. At the same time, the recent literature suggests that some caution is warranted about linking policy changes and growth with poverty outcomes,

⁴¹ *From Adjustment Lending to Development Policy Lending: Update of World Bank Policy* (R2004-0135), July 15, 2004.

⁴² *Good Practice Note on Designing Development Policy Lending*, OPCS, World Bank, 2004, and Stefan Koeberle, “Should Policy-Based Lending Still Involve Conditionality?” *World Bank Research Observer*, Vol. 18, no. 2 (2003), pp. 249-273.

since the knowledge on the (time-specific and context-specific) determinants of growth and poverty is fairly weak.

- ***Additionality.*** It has become increasingly accepted that the Bank’s support should be based on the country’s own policy program rather than leverage additional and perhaps more ambitious policy reforms. The Bank’s “additionality” is thus embedded in its analytic and advisory services, which help the country develop policy options, and in its financial services, which support the implementation of programs.
- ***Medium-term framework.*** The Bank’s operational policy asks that development policy lending be built around medium-term institutional and structural actions that are driven by the country itself, and that it aim to promote growth, improve social conditions, and reduce poverty.

V. SUGGESTED KEY ISSUES FOR THE CONDITIONALITY REVIEW

22. One objective of the conditionality review will be to describe recent trends and changes and assess their significance for the use of conditionality. But it will also provide an opportunity to explore important issues that are currently being discussed by the development community, including bilateral donors.

- ***Improving predictability.*** A major concern in LICs receiving significant budget support is the predictability of that assistance. Unpredictable fiscal cash flows can lead to macroeconomic instability or inefficient expenditure allocation and execution, especially when budget support amounts to a significant share of government inflows. Moreover, given that the Millennium Development Goals (MDGs) are a long-term agenda, the terms at which aid flows are committed gain particular relevance. What is the best way to ensure the predictability of budget support for LICs in the context of potentially larger aid inflows for achieving the MDGs? How could the predictability of resource flows minimize the risk of aid dependence, unsustainable government finances, and moral hazard? When is it appropriate to finance budget support through grants or debt-creating lending? What are appropriate and effective criteria and processes for responding to inadequate country performance? What is the experience with different mechanisms that allow for a graduated and less disruptive response in such cases? What can the Bank learn from the variable tranche approach espoused by the European Commission, which proposed to guarantee at least part of the following year’s support regardless of country performance?
- ***Improving donor harmonization and support for country-owned strategies*** The increased efforts toward donor harmonization of budget support have had positive effects, but have also raised some issues for the implementation of conditionality. As more donors participate in the design of a unified program, there may be a risk that the number of conditions will rise while the quality and relevance of the substance suffer. Moreover, the fact that some donors use

political conditionality in those unified policy matrices has in some instances placed the Bank in an uncomfortable position, given that its Articles of Agreement prohibit political interference.⁴³ How can conditionality be structured to best support a mutual agreement with donors and recipient governments on a country's own poverty reduction strategy (PRS)? When is it appropriate for donor-supported policy programs to move beyond the details of the PRS? Does donor harmonization necessarily imply a unified policy matrix, or could there be a division of labor based on expertise? How can donor harmonization reduce the risk of sharp curtailments of budget support flows in case of inadequate performance? When is poverty and social impact analysis (PSIA) a useful tool for ensuring that the PRS, from which conditions or benchmarks are derived, is based on clear evidence of benefits to the poor and has widespread buy-in?

- ***Operationalizing a results framework.*** To the extent that national PRSs are well articulated and prioritized, the presentation of a policy program to be supported by the Bank can rely on existing policy matrices. Since this is not always the case, governments have frequently found it useful to have Bank assistance in operationalizing a more detailed results framework—particularly when it serves as a vehicle for substantive sector dialogue. Such presentation in the program documentation have sometimes been criticized as intrusive micromanagement that is inconsistent with national PRSs. What are the good practice experiences in separating such results frameworks from actual conditionality?
- ***The scope and content of conditionality.*** Experience with policy-based reforms in sensitive policy areas such as privatization, trade liberalization, user fees, and fiscal policy has been mixed. What does the effectiveness of such policy reforms suggest about the scope and appropriate circumstances for the use of this kind of conditionality? The lessons of the 1990s show that generalized policy prescriptions and blueprints are inappropriate—but key principles may still be valid and should be derived from the specific country context. What does this imply for the practice of conditionality?
- ***Appropriate level for application of conditionality.*** When should conditions be best applied—at the level of individual operations and interventions or at the level of the entire country program through the CAS? Could a distinction among fiduciary, process, and policy conditions help focus on the critical conditionality for policy-based lending? How can conditionality be better customized to the different circumstances of the Bank's client countries, ranging from low-income countries under stress (LICUS) to PRSP countries and middle-income countries? What is the appropriate type of conditionality

⁴³ IBRD Articles of Agreement, Article 4, Section 10; and IDA Articles of Agreement, Article 5, Section 6.

suggested by experience for different situations, such as rapid crisis and shock response, contingent countercyclical financing, or regular budget support?

- ***Conditionality in fragile states.*** The World Bank and other donors have been providing budget support for poverty reduction and reconstruction in fragile states such as Afghanistan, Timor Leste, and in West Bank/Gaza. While the Bank's LICUS approach has provided a framework of engagement with fragile states, it would be useful to review lessons of good practice—and bad practice—emerging from the experience with conditionality in policy-based lending in fragile states. In post-conflict transition situations, there are some good examples of the use of policy-based lending to structure donor dialogue on priorities and leverage complementary capacity building. Should the Bank be more focused in the use of conditionality where capacity is weak? What mechanisms can be put in place to achieve a minimum acceptable level of fiduciary control in a fragile environment? How should policy-based programs, particularly in post-conflict countries, address transitional priorities across the political, security, economic, and social spheres? Should there be a clearer distinction between countries where the government lacks capacity versus countries where the authorities are unresponsive to development issues?

23. ***Different Country Circumstances.*** For many of these issues and questions there is no unique answer. To a large extent, the relevance of the issue and response seems to depend on the specific circumstances of the country. It would be unduly narrow for the conditionality debate to be limited to the notion of regular budget support for a well-performing low-income country. Clearly, the approach to conditionality would be expected to vary a great deal depending on whether it is applied to middle-income countries, low-income countries, and low-income countries under stress or fragile states and post-conflict countries. Similarly, it would be unrealistic to suppose that recipient countries are mostly functioning democracies that are able to respond to the interests of the majority of the population, avoid elite or foreign-interest capture, develop completely uniform positions within government on all difficult issues, and maintain a stable course on reforms. In such a world, foreign aid agencies could simply finance country programs without any suggestions of conditionality. This of course is not the reality in many countries where donors deal with governments that are fractured and not fully representative, where one part of the government may be asking for conditionality in order to hem in dissenting parts,⁴⁴ and where today's commitment can turn into tomorrow's disappointment. A more nuanced assessment of the lessons for the use of conditionality seems warranted for this review. To better understand how the practice of conditionality might vary, it may be useful to approach the range of specific country circumstances through a combination of different criteria:

⁴⁴ Some observers point out that this kind of conditionality dilutes domestic accountability of policymakers to the extent that governments can blame external partners for policy failures.

- ***Implementation capacity and aid dependency.*** The set of borrowing countries ranges from those that have a limited capacity and resource endowments, are highly aid-dependent, and need a greater degree of technical assistance from the Bank to those that are at the cutting edge of policy design and implementation, enjoy ready access to financial markets, and are at the brink of graduating from using Bank resources.
- ***Degree of commitment and reform readiness.*** Aid recipient countries range from those with ineffective governments that are driven by internal dissent and conflict and can barely define a course of action, to those that have a clear sense of direction and implement a realistic and sustainable policy program that enjoys broad support by stakeholders.
- ***Effectiveness of resource use.*** Recipient countries also range widely in terms of the efficiency with which they use their resources. At one end of the spectrum, the effectiveness of policy implementation and the use of fiscal and public resources may be so weak that scaling up resource flows is unlikely to yield any significant outcomes. At the other end of the spectrum, some countries make the most out of their resource endowment—human, natural, and financial—and a small amount of support could potentially leverage significant outcomes.
- ***Fiduciary framework.*** The settings and institutions used by borrowing countries to handle their foreign reserves, fiscal resources, and procurement also vary widely. Few countries have completely dysfunctional fiduciary systems without fiscal transparency or public accountability, or completely sophisticated and transparent public financial management systems; most recipient countries fall somewhere in between.
- ***Macroeconomic and financial vulnerability to crises.*** There is also a broad range of country vulnerability to adverse macroeconomic and financial crises. In some countries external shocks occur with some frequency, often resulting in severe negative repercussions for the economy, the financial sector, and poor people. Other countries have developed a certain macroeconomic and financial resilience that renders them less susceptible to lasting negative repercussions of temporary shocks.

VI. WHERE SHOULD CONDITIONALITY GO?

24. This review is an opportunity to revisit the Bank's approaches to conditionality in policy-based lending and suggest improvements. It may encourage the Bank to build on the progress of recent years in streamlining conditionality and using programmatic approaches for greater flexibility and medium-term support. The review is also likely to emphasize the importance of continued progress in aligning more closely with national policy programs and country processes and budget cycles, and harmonizing with bilateral donors, particularly in low-income countries.

25. ***Beyond Conditionality.*** The conditionality review could help formulate suggested good practice principles for the Bank’s future use of conditionality in policy-based lending, in a way that can be monitored. It may be appropriate to ask whether conditionality has changed to such an extent that it is no longer commonly understood to mean the same thing to most people. A broadly agreed concept of conditionality would be a useful contribution of this review. Perhaps the time has come to recognize the ongoing move beyond traditional conditionality by substituting a more pragmatic term such as “support for policy reform,” “compact,” or “results partnership.”

26. ***Questions for Good Practice Principles.*** Guidance from Executive Directors, staff discussions, and feedback from borrowers, other donors, civil society organizations, and interested parties will help in the formulation of suggested good practice principles, which could make the relevance and usefulness of the Bank’s approach to conditionality more appropriate. Some of these good practice principles for the Bank’s future use of conditionality may build on key concepts that have emerged from the analytic and review work carried out thus far, and on what has already been recognized in operational policy and good practice.⁴⁵ But the review would also permit drawing on suggestions and experiences from other development partners on how to best reconcile the tensions among different aspirations. Three types of considerations for policy-based lending might provide a possible framework: selectivity criteria, design criteria, and implementation objectives.

27. ***Selectivity Criteria.*** Selectivity criteria for determining whether to support specific elements of a country’s program would involve guidance on navigating the tensions between the objectives of country ownership and the Bank’s mandate to exercise due diligence on aid effectiveness and fiduciary responsibilities.

- What is a practical way to determine ownership? Is the country’s track record a sufficient indicator?
- How can the Bank best reconcile the tension between the objective of country ownership of a policy program and its obligations for due diligence?
- How can the Bank assure its shareholders that a country’s fiduciary arrangements are adequate and its financial support is used for the purposes intended? Is selectivity the appropriate response if the country’s track record, implementation capacity, and fiduciary arrangements are less than fully adequate?
- When the Bank’s expertise suggests that a country’s policies in an otherwise acceptable program are ill-advised and detrimental for the achievement of the country’s objectives, should the Bank attempt to use conditionality to change the country’s approach or should it rely on analytic work and refrain from

⁴⁵ *Good Practice Note on Designing Development Policy Lending*, OPCS, World Bank, 2004.

policy-based lending? Or is it more effective to stay engaged through a narrower policy program that excludes controversial areas?

- How can the Bank use its knowledge and experience to help developing countries evaluate different policy options? Should Bank explicitly discourage attempts to leverage additional reforms through policy conditionality beyond the country's own original program?
- Should programs focus only on those policy actions that are truly critical for the implementation and achievement of key results? How should this be determined when the knowledge of attribution and causal chains is limited?
- Should the criticality of actions differ depending on country circumstances and whether the country is a LICUS, a LIC, or a middle-income country (MIC)?
- Can an external frame of reference (such as European Union accession) provide sufficient development effectiveness and fiduciary assurance for other development partners to substitute for conditionality?

28. ***Design Criteria.*** Design criteria for determining the appropriate form of support would need to acknowledge the tension between the objectives of flexibility and results orientation.

- How can the timing of the results framework for policy-based lending best correspond to a realistic assessment of the time required for implementation? When is a medium-term framework appropriate? How should conditionality be designed in crisis situations?
- When are multitranche or programmatic most appropriate?
- For multisector policy programs that cover a broad array of areas, how can lengthy and complex policy matrices be made more manageable?
- What does the experience suggest about the reliance on outcomes instead of specific policy actions such as benchmarks, triggers, or conditions?
- How can the policy program be best aligned with the poverty reduction strategy of a LIC? To what extent can the policy matrix depart from a PRSP that is not sufficiently prioritized, operational, or specific?
- How can the Bank make greater use of analytic underpinnings to encourage deeper engagement of relevant stakeholders in their discussion and adoption?
- Should the Bank frame its support within a programmatic approach that is based on the track record of actions already taken? Should it clarify that triggers are a small set of indicative expected prior actions to help assess

future support, with the understanding that they can and will be adapted whenever circumstances warrant?

- For a given policy program, what is the difference between policy, fiduciary, and process conditions? How relevant is each type?

29. ***Implementation Objectives*** Implementation objectives would need to help reconcile the tension between the predictability of resource flows and an assessment of country performance.

- In the interest of resource predictability, should the Bank's support be implemented with a great degree of flexibility to adapt policies to changing realities and observed outcomes, as long as overall program implementation remains broadly on track? How should this overall judgment be made, and how can it avoid giving the recipient country a sense of entitlement to financing flows?
- What is the appropriate response in case of inadequate performance? If reductions in financial support are preferable to delays in disbursing the loan, should they typically be of a magnitude that does not jeopardize the country's development progress?
- How can donor harmonization be promoted without an undue burden of conditionality and resource volatility for the recipient country? To what degree should the timing and extent of the Bank's response to inadequate performance be harmonized with other donors in LICs? What does experience suggest about the use of variable tranches as a way to make resource flows more predictable?
- What are the appropriate benchmarks for determining whether a program is sufficiently offtrack that financial flows should cease altogether?
- How can the implementation of effective policy programs be governed by increased transparency, through a greater involvement of parliaments and representative bodies, and through the empowerment of weaker groups who are supposed to benefit from development—with due consideration of the restrictions on political interference imposed by the Articles of Agreement?
- How can the Bank's policy support better rely on the country's own systems, in particular the country's monitoring arrangements and the systems related to the management of budget resources and foreign reserves?
- How can the Bank most effectively fulfill the obligation to its shareholders to evaluate whether it is sufficiently satisfied with program progress to provide further financial support? In reporting to the Bank on program progress, to what extent can a country draw on its own reporting mechanism for

monitoring and evaluation, such as reporting annual budget outcomes to parliament?

VII. PRELIMINARY WORK PROGRAM

30. The conditionality review will be a comprehensive, inclusive process that will take place during FY05. While the ultimate output is a report for the Development Committee in September 2005 and operational guidelines for staff, interim deliverables will be a set of policy papers to be prepared for discussion by Executive Directors.

31. *Feedback from Borrowers and External Stakeholders.* There will be a number of consultations with borrowers, as well as discussions with other development agencies, bilateral donors, and civil society organizations. These consultations will be complemented by a survey of borrowing country government officials—past and present—to elicit their key suggestions for the practice of conditionality.⁴⁶ In addition, the Bank has set up a discussion-based external website specifically designed for the review, to which interested parties are invited to contribute.⁴⁷ The external consultations are set out in Table 1, starting with a roundtable with donors and nongovernmental organizations (NGOs) hosted by the Department for International Development (DFID), which took place in London on December 13, 2004. Where possible, the program will build on specific events that are already scheduled for other purposes. It includes a discussion to be held in Berlin in March under the auspices of the German Government, where the key participants will be government officials and civil society organizations (CSOs) from borrowing countries.

⁴⁶ The survey will be carried out through a web-based service that will allow access to only those invited and will guarantee the anonymity and confidentiality of the responses. The survey will be structured to allow quantification of the results.

⁴⁷ The discussion-based consultation website will change focus every month, calling for contributions on the following four topics: ownership, criticality, additionality, and medium-term framework.

Table 1. Tentative List of External Discussions for Conditionality Review

<i>Date</i>	<i>Location</i>	<i>Host</i>	<i>Objective</i>	<i>Participants</i>	<i>Materials</i>
<i>December 13, 2004</i>	London Roundtable	UK (DFID)	Seek feedback on concept of conditionality review	Donor representatives, academics, aid agencies, and civil society organizations	<ul style="list-style-type: none"> • Draft issues paper • PowerPoint on updated trends
<i>January 12, 2005</i>	London LICUS conference	ODI (in conjunction with the LICUS meeting)	Discuss conditionality in fragile states	Recipient governments, academics, donors, and NGOs	<ul style="list-style-type: none"> • Draft note on fragile states
<i>February 2005</i>	Video-conference	World Bank	Discuss the practice of conditionality from the perspective of MDBs	Multilateral development banks	<ul style="list-style-type: none"> • Issues paper
<i>March 2005</i>	Berlin	Germany (InWent)	Consultation with selected borrowers	Borrowing countries, NGOs from those countries, and aid agencies	<ul style="list-style-type: none"> • Issues paper • Draft trends paper
<i>April 2005</i>	Video-conference	World Bank	Consultations with parliamentarians of borrowing countries on conditionality	Bank's Parliamentary Network	<ul style="list-style-type: none"> • Issues paper
<i>Spring 2005</i>	Spring Meetings	World Bank	Consultation with MICs	Governments and main CSOs of G24	<ul style="list-style-type: none"> • Issues paper • Draft trends paper
<i>Spring 2005</i>	Spring Meetings	World Bank	Consultation with LICs	Governments and main CSOs of LICs	<ul style="list-style-type: none"> • PRSC stocktaking paper
<i>Spring 2005</i>	Spring Meetings	World Bank	Consultation with NGOs	International CSOs	<ul style="list-style-type: none"> • Issues paper • Draft trends paper
<i>May 5/6, 2005</i>	Cape Town Practitioners' Forum on budget support	World Bank/SPA		PRSP borrowing countries, CSOs from PRSP countries, academics, and aid agencies	<ul style="list-style-type: none"> • Set of papers commissioned for seminar

32. **Bankwide Conditionality Panel.** A Bankwide panel of staff has been convened to provide guidance throughout the conditionality review process and to review early drafts of the various policy papers. The panel consists of a wide range of experienced managers and development practitioners across different Regions and Networks.

33. **Proposed Analytic Work.** The substance of the conditionality review will be reflected in analytic work and policy papers that will build to the extent possible on the consultation discussions. They will be submitted to Executive Directors for discussion in the course of FY05. A final Board paper summarizing and drawing the main conclusions for discussion by the Executive Directors would be discussed with the Board in draft and in a formal Board meeting by the end of July 2005, before the summer break. A preliminary list of papers and contributions is set out in Table 2, in the tentative order of preparation.

34. **Upstream Engagement of the Board.** Executive Directors will be invited to formally discuss the different papers that will be prepared in the context of the review, starting with this issues paper and ending with an overall Board paper (see Table 2). The review may also benefit from a candid exchange of ideas on the key issues in the context

of an informal seminar, perhaps in the form of an off-site retreat. The seminar, which could be scheduled for the spring of 2004 if Directors agree, could lay the ground for the position paper that would be discussed by the Board as the basis for the report that will be presented to the Development Committee.

35. *Development Committee.* The final objective is to send to the Development Committee a concise paper summarizing the conclusions. This summary, to be ready by August 2005, will draw on the Chairman's Statement following the discussion of the topic by the Executive Board. On the basis of the discussion at the Development Committee, the Bank would conclude the conditionality review by issuing to staff a set of monitorable operational guidelines, refined during the review, that would embody the principles for moving beyond conditionality.

Table 2. Tentative List of Analytic Work for Conditionality Review

<i>Contribution</i>	<i>Tentative date</i>	<i>Principal author</i>	<i>Objective</i>
Issues Paper	February 2005	OPCCE	<ul style="list-style-type: none"> Set out concept of conditionality review
Results in Development Policy Lending	February 2005	OPCCE	<ul style="list-style-type: none"> Good practice in achieving a results-orientation in policy based lending (including separating it from conditionality)
Modalities of Bank Conditionality	April 2005	OPCCE	<ul style="list-style-type: none"> Principal forms of conditionality (conditions, prior actions, triggers, difference from CAS triggers, etc.). Role of and scope for using outcome-based conditionality in Bank conditionality, review of variable tranches Information on the financial conditions of Bank support
PRSC Retrospective	April 2005	OPCCE	<ul style="list-style-type: none"> Review experience with PRSCs
Trends in policy-based lending	April 2005	OPCCE	<ul style="list-style-type: none"> Update of trends in numbers and content of conditionality Overview of aggregate Bank-Fund conditionality Draw on analysis in Adjustment Lending Retrospective and Programmatic Adjustment Lending Retrospective
Conditionality in fragile states	Spring 2005	OPCCE-LICUS	<ul style="list-style-type: none"> Good practice in budget support for fragile states
Content of conditionality	April 2005	PREM	<ul style="list-style-type: none"> Lessons of 1990s on Washington Consensus Analysis of policy reforms in (i) privatization, (ii) trade, (iii) user fees, and (iv) fiscal policy.
Poverty and Social Impact Analysis within the PRS Progress Report	Summer 2005	PREM	<ul style="list-style-type: none"> Status of PSIA work Linkages between PSIA and policy-based lending
Literature review	April 2005	DEC/PREM	<ul style="list-style-type: none"> Review of recent analytic contributions Summarize academic literature and its recommendations
Summary of consultations	July 2005	OPCCE	<ul style="list-style-type: none"> Including LICUS, selected borrowers, LICs, and MICs
Conditionality Review Board Paper	July 2005	OPCCE	<ul style="list-style-type: none"> Summarize conclusions of conditionality review Set out future operational principles to move from conditionality to country-driven results partnership