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

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Mr. Aleksei Kudrin
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to the Joint Ministerial Committee of the Boards of Governors
of the World Bank and the IMF on the Transfer of Real Resources
to Developing Countries (Development Committee)

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Implications of the Global Economic Crisis for Developing Countries and the Role of International Financial Institutions

The circumstances surrounding this meeting of the Development Committee call for self-reflection and decisive action. I suggest that from now on, the Development Committee should regularly discuss systemic risks to the global economy and what needs to be done to manage them responsibly. Some of those risks derive from the situation of development emergency associated with re-emerging absolute poverty, worsening social indicators, and possible political unrest. For the first time since the World War II we face the contraction in global economic growth and trade. The situation is aggravated by drastic reduction in private capital flows to the developing world, including freeze in cross-border bank finance, and sharp decline in remittances.

We understand that different groups of countries are in different state with respect to providing counter-cyclical fiscal stimulus to their economies. Furthermore, emerging and developing countries differ in their ability to address current challenges depending on their pre-crisis fiscal and balance of payment positions as well as quality of macroeconomic policies. An effective fiscal and monetary stimulus could be afforded only by those who had sustainable fiscal balances and sufficient reserves. As a result, the developing world is largely the weakest link in our collective response to the global crisis. We strongly believe that developing countries can and should be part of the solution.

Large stimulus packages adopted by some developed countries imply a heavy reliance on growing budget deficits to be financed by huge increases in national debt. That, by the way, will further inhibit the ability of emerging and developing countries to access international capital markets.

One of the most important options in terms of providing a meaningful anti-crisis response in developing countries is associated with the enhancement of the multilateral financial institutions, including multilateral development banks (MDBs). As emphasized by the presidents of major MDBs at the G-20 Summit in London, the role of their banks as a source of predictable and affordable financing that can leverage substantial funds at very limited costs to shareholders is significant.

Yet, there are some issues of strategic nature that will determine whether the MDBs will be able to play their designated role in this response. Serious financial constraints met by many of MDBs raise doubts in their ability to deliver on a looked-for scale. The World Bank is already using their capital at a rate not previously expected. While there may be some room for maneuver through increase in leverage ratios within existing capitalization, we would not regard this as a sustainable way of dealing with the issue. After all, excessive leveraging is one of the key reasons of the current crisis.
In this context, we should not exclude the option of considering a general capital increase for the World Bank at some point in time. Without fresh resources, some MDBs, especially those dedicated to private sector support, will find their lending room constrained in a not so distant future. The net incomes of IFC and EBRD are already crossing into negative area. As a way forward, it might be useful to evaluate prudential ratios and capital adequacy of all multilateral development institutions thereby enhancing their transparency and comparability of financial reporting.

Another critical issue for the MDBs is the availability of effective counter-cyclical instruments at their disposal. These should be flexible, fast disbursing instruments designed to provide substantial front-loaded assistance to developing countries facing financing gaps in the context of the current crisis. The list can include traditional fast-track instruments that MDBs can deploy under streamlined operational procedures. The MDBs should continue to simplify their operational procedures, progressively increase utilization of the country systems and the speed of reviewing client requests and preparing projects.

MDBs should use innovative approaches to assist countries in dealing with market volatility such as local currency borrowing, hedging facilities, risk-sharing arrangements with public and private donors and creditors, guarantees for credit enhancement including those for government issuances, and sub-sovereign lending. To address grim situation faced by many partners we should not shy away from any unconventional solution to maintain short-term trade finance for poor countries.

Direct support to the private sector and the use of MDBs’ balance sheets for mitigating risks and catalyze private sector flows to the developing countries should be regarded as an integral part of the global anti-crisis action. Without a strong response from the private sector, the growth in global economy will not resume. There are various ways, in which MDBs can effectively step up support to private sector. They include:

- guarantees to facilitate bond-issuance;
- encouragement of private and public investments in infrastructure;
- bank recapitalizations;
- advisory and financial assistance to investors from developed and emerging economies who are willing to enter poorer markets in difficult times;
- refinancing by means of syndicated instruments, under which e.g. IFC lends not only its own funds but also funds mobilized from other participants;
- trade finance.

We welcome the efforts of the World Bank Group to this end and expect the results of the thorough review of its capital adequacy in the near future to make sure there are sufficient resources for scaling-up.

We welcome the work done by the World Bank so far on its Vulnerability Financing Facility, particularly the establishment of the Rapid Social Response Program. We appreciate highly flexible design of these operations accommodating various needs, interests, and specific situations in member countries. We intend to contribute funds to the Vulnerability Financing Facility based on the assumption that in utilizing our contribution the Bank will take into account our geographic and sector priorities.

In this context, we would like to note that Russian Federation is providing assistance to a number of crisis-hit countries, particularly within its region. Since the second half of 2008, Russia has extended to Belarus $2 billion in stabilization loans. Agreements have been reached to provide a $2 billion loan to the Kyrgyz Republic and a $500 million stabilization loan to the Republic of Armenia. In addition, Russia will contribute $7.5 billion to the proposed $10 billion Eurasia Economic Union Anti-crisis Fund that will be established by Armenia, Belarus, Kazakhstan, Kyrgyz Republic, Russian Federation and Tajikistan. Some other additional measures are being considered.
Voice and Participation

We welcome the progress that the World Bank and its shareholders have made on the voice and participation reform since the 2008 Annual Meetings. We appreciate the constructive spirit, in which our colleagues have reached the compromise and thank the World Bank management for facilitating the intense consultations that preceded the approval of the package. We consider the first phase of reform an important and positive development, even though we recognize that it is proceeding without sufficient clarity with respect to its objectives and strategy.

We hope that the proposed increase of basic votes to 5.55 percent of total votes accompanied by the notable allocation of 7,117 unallocated shares to sixteen DTC members; and adding an additional Executive Director to represent Sub-Saharan Africa, will strengthen the DTC’s say in and contribution to their own and global development.

As we stated before, the success of the voice and participation reform should be judged by incentives that it creates:

- for the DTC to accelerate their development;
- for the developed countries to provide development assistance to the DTCs, and
- for both, developed counties and DTCs to join forces in tackling global challenges.

The current financial and economic crisis has confirmed that we cannot rely on the wisdom and experience of the developed countries alone to shield the world from such serious setbacks. The developing and transitional countries that had little control over the factors that triggered the crisis are now bearing heavy economic and social costs. The world needs more mutual accountability, and greater voice and participation of the DTCs in the affairs of the World Bank is one way to provide it. This is why we have joined other countries in supporting the voice and participation reform at the World Bank.

The next phase of reform represents a greater challenge for all of us. First, the voice and participation reform agenda is competing for the attention of decision-makers with the anti-crisis agenda, which, arguably, is more critical, at least, in the short run. Second, there are no more authorized but unallocated shares that could be used for offsetting shareholders’ loses of voting power.

The voice and participation reform will work only if we design it to deliver what it promises. However, if the scope of reform is limited to a reallocation of shares, it will be unable to deliver the promised results. In an organization, where the shareholders do not feel they have enough voice to provide the necessary oversight and policy guidance, redistribution of votes among them will not make a meaningful difference.

Internal governance reform and enhancing participation of developing and transition countries in the World Bank Group requires:

- increasing staff and management diversity that should be supported by more insightful recruitment and more effective on-boarding programs;
- stronger engagement of clients into design and implementation of the Bank-supported programs;
- unrestricted and merit-based selection of the President; and
- decentralization, whenever there is a business case for it.
We consider parity between the DTCs and developed countries a notion that needs to be judged in a context. At this stage of reform, it points us in the right direction. However, we believe that the ultimate objective of the voice and participation reform, against which all its principles and targets should be measured, is maximizing development effectiveness of the World Bank.

We look forward to the second phase of reform that needs to be development mission-oriented, inclusive, transparent, principle-based, realistic, and should strike an appropriate balance between its pace and the quality of the reform process.