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Transfer of Resources for Development

The transfer of financial resources to the developing countries and transition economies, on the whole, continues to show a positive trend. However there is a certain concern over the fact that dynamics of private capital inflows is still not commensurate to the global economic growth. It is in this context that we are talking about the catalytic role of the international financial institutions, which must set an example by extending investments to a wider range of countries and sectors.

We note the traditional importance of foreign direct investment—the most sustainable and reliable component of external financing. Direct investment has the greatest impact on medium- and long-term trends in economic development. We must point out in this regard that, according to Bank's data, direct investment to developing and transition economies has dropped sharply as a proportion of total cross-border direct investment worldwide. This clearly indicates that while the global supply of funds for direct investment is growing, the relative attractiveness of developing countries is declining. Therefore recipient countries should not dwell on their past achievements; instead, they should accelerate the process of macroeconomic and structural reforms, including those in foreign trade, labor relations, financial sector, infrastructure, and regulatory area.

Poverty Reduction and Global Public Goods

We have studied with interest the Bank's proposals on global public goods. Research in this area should continue. Bearing in mind that examination of this issue is at a very early stage, we would like to make a number of preliminary points:

1. Conceptually, the notion of global public goods has both appealing characteristics—primarily its emphasis on cooperation and partnership—but also raises issues of concern. Among the latter is the well-known fact that it is extremely difficult to come up with a workable definition of "public goods." On the one hand, virtually any good involves a number of externalities that allow it to be portrayed as requiring collective action. On the other hand, a significant share of what traditionally belongs to the domain of public sector is also provided by the private sector in a number of countries and cases. Moreover, even when there is a more or less sustainable consensus about a set of "public goods", including global ones, this concept does not provide any tools for setting priorities among them. As a result, the decision about what should be supported through international collective action, and how, is made in a discretionary and politicized manner, which substantially depreciates the validity of this approach itself.

2. Traditionally the concept of "public goods" is directly linked to their funding with government resources. The customary view is that territorial certain public goods (local, regional or national) require taxation at a corresponding level, and that the accumulated public funds should be used to produce this good for general use, free of charge or on a subsidized basis. It's no accident that the proposed document effectively raises, albeit with reservations, the issue of global, i.e. supranational, taxation and the establishment of corresponding governing bodies. It should be clearly understood in this context that supremacy of the national sovereignty of member countries is uninfringeable. Any discussion about the "world government" and "global

taxation” can only lead to unnecessary confusion. There is no room for that within the Bretton Woods institutions.

3. If we try to translate the half-century experience of the international financial institutions into the vernacular of “global public goods”, we should acknowledge that the most important, most widespread and effective public good they produce, that has the greatest positive global effect, is the actual process of accelerated economic growth. When a country moves up to a higher level of economic development, the inevitable result is that issues we promote, such as environmental protection, public health, living standards, equal participation in civil society, and so forth, become more prominent among other public priorities. And if all agree that poverty reduction is the key problem of our time, it’s no coincidence that the most dramatic successes in this area in recent decades have been achieved by countries that have been able to produce the highest and most sustainable economic growth.

Consequently, there is every reason to assert that the World Bank’s mandate as an institution that promotes sustainable economic growth is in itself a unique and most valuable global public good. There is absolutely no contradiction between an orientation toward global public goods and the Bank’s traditional country focus, which has been recently reflected in the Comprehensive Development Framework (CDF) and in the affirmation of the country’s priority in the dialog with the Bank.

However, the vast increase in partnerships and the Bank’s participation in international programs is fraught with danger of politicization and discretion. We welcome the fact that these points are clearly made in the Bank’s report. In our view, these areas of activity must not and cannot become the top priorities for the Bank. Their role must remain subsidiary as compared with providing assistance to member countries at their request and in line with their national priorities. In this context one should avoid pitting these national priorities against the International Development Goals. The latter must not become the equivalent of the centralized directives that were once typical of the command economies. The role of these goals is indicative, illustrative, catalytic, but not operational.

As for the main areas of the Bank’s participation in the current division of labor on development assistance, they seem to be adequately defined. We especially welcome the increased attention to the problem of epidemic diseases—tuberculosis and AIDS in particular—which in a number of cases is assuming regional and global importance.

Improvement of economic management has also been included, quite properly, among the most important areas in which the Bank’s comparative advantages are especially prominent. Among other things, we fully share the concern voiced about the high cost of doing business with international development banks. The World Bank recently began its own internal study of this problem. If the Bank can achieve noticeable improvements in this area, this will serve as an excellent example of a global public good.

Since the Bank raises the concept of global public goods for the first time, a number of questions naturally need clarification. For one thing, it’s not quite clear why the issue of inadequate banking supervision has been combined with the problems of money laundering and the fight against corruption. It seems that the objectives of banking supervision are much broader and more multifaceted than prevention of criminal activities. It's equally unclear whether the free cross-border movement of goods and capital should be placed on the same footing with unrestricted labor mobility. While liberalization of trade and of capital movement pertains mainly to economics, the movement of population across the national borders brings about a large number of complicated social, cultural and political problems. In our view, it is too early to initiate a global debate on this issue.

The issue of collective action inevitably raises the problem of financing. It seems to us that the Bank should continue to follow the time-tested principles of its participation in funding these operations: focused selectivity, strong catalytic effect, large-scale co-financing from partners and overall subordination to the national strategies of participating countries.

In any case, the Bank's participation in these programs must not result in hardening lending terms and conditions within the framework of its primary mandate. If incremental costs of collective action are passed on to the borrowers, this will inevitably lead the Bank into a dead end. We believe that this issue cannot be a matter of discussion.

World Bank Role and Instruments in Low- and Middle-Income Countries

In our view the report on the role and instruments of the World Bank as also an interesting, promising initiative. The report does not so much propose solutions as it summarizes the problem and makes new suggestions regarding future directions of the Bank's strategic development. We are counting on the Bank's Board of Directors to continue the examination of these problems and to devise balanced, productive solutions.

However, we can already make the following points.

In regard to **the IDA-eligible countries,** closer attention should be paid to their opinion about proposals to introduce a generalized linkage between the CAS and the PRSP processes beginning on July 1, 2002.

First, the PRSP mechanism was originally proposed for very specific purpose, namely to provide debt relief under the HIPC Initiative.

Second, the very philosophy of this mechanism presupposes that the borrowing countries will participate much more actively in its design and preparation. Therefore, it doesn't seem quite logical to impose this mechanism too forcefully on the countries themselves. The specific situations of these countries are too varied — from countries with huge populations, complex federal structure and historical traditions in drawing up government programs, to the tiniest island states with extremely limited institutional capacities. It is completely inappropriate to automatically apply a uniform approach in this case.

On the whole, we support the proposal to develop the PRSC. The positive aspects of this instrument are based on the linkage between its medium-term programmatic nature and the borrowing country's budget cycle. We would not particularly emphasize the parallel between this instrument and the IMF's PRGF. It certainly isn't the Bank's objective to create instruments that compete with or replicate IMF instruments. Naturally, the PRSC should be considered when, among other things, appropriate macroeconomic policies are in place. Ability to fully meet the PRGF performance criteria can and should be the most commonly accepted evidence of compliance with this requirement, but special cases are also quite possible. In each concrete situation a solution must be found in the course of intensive cooperation between the World Bank and the IMF, as previously mentioned.

As for **IBRD-borrowing countries,** the situation merits closer study. It's no secret that the international community's attention in recent years has been focused more on the poor countries' problems. As a result, analysis of the problems of middle-income countries has lagged somewhat. We therefore whole-heartedly welcome the creation of a special task force to examine these issues. We expect a fairly detailed report on its findings by the time of the Development Committee's spring session.

In our view, this report should reflect the following propositions and principles:

1. A CAS that combines the borrowing country's priorities and the Bank's sector strategies should remain the key instrument of the country's cooperation with the Bank. This requires that the borrower country's ownership of the strategy be consistently expanded.

2. The composition of the lending program should combine investment projects, budget loans and loans for technical assistance in an balanced manner. The final word on the composition of country lending should belong to the borrowing country, and it should take into account the limitations imposed by the Bank's general policies.

3. The Bank should expand its menu of lending instruments. To achieve the strategic goal of strengthening market economies and links to the private sector the Bank's menu should be shaped accordingly, including more active use of guarantee operations. We should point out that, even though it has been five years since the decision was made to include guarantee operations into the Bank's standard menu of instruments, the results have still been less than modest while the demand for this product remains high.

4. It's imperative that the programmatic approach that has been started with respect to investment loans be extended to budget lending. Furthermore, the implementation of agreed programs should be evaluated not by relying on intermediate results that reflect the process of program implementation, but by using the indicators that measure goal attainment. We are very interested in the proposals to develop a new instrument, provisionally called the DSL, which will be used in coordination with the borrowing country's budget cycle.

5. The full potential of the World Bank Group should be used to promote development of the private sector. We would like country directors to manage operations of all the institutions within the World Bank Group in the country. This would result in actual substantive coordination and cooperation among the IBRD, the IFC and MIGA.

6. The issue of the cost of doing business with the Bank should be separated from that of the Bank's operational model in the IBRD borrowing countries. This issue should be considered in the context of developing Bank's financial instruments, trends in its financial condition and the demand for the Bank's financial products. The demand for these products depends increasingly on the constantly growing hidden elements in the cost of doing business with the Bank. All of the World Bank Group's borrowers feel this problem, but it is especially severe for IBRD borrowers. Specifically, it should be given top priority when the new instrument, the Development Support Loan, is devised.

7. In order to assist middle-income countries efficiently, the Bank, in addition to its traditional role of intermediary in transfer of financial resources, should develop new areas related to the development and transfer of knowledge. This requires a special emphasis on modern information technologies. A promising example here is the Global Development Gateway that the Bank is working on. The inevitable budgetary consequences of this work can be mitigated by paying increased attention to the use and development of local capacities.

The Comprehensive Development Framework (CDF)

We support the fundamental principles and objectives of the Comprehensive Development Framework introduced by World Bank President Wolfensohn in January, 1999. The experience of the first few months of CDF implementation in a number of countries that decided to take part in its pilot stage confirms that the direction chosen was the right one. In a short period of time most of these countries have achieved noticeable progress in formulating a long-term vision of the challenges of national development. This vision gives balanced attention to macroeconomic, structural, institutional, physical, social, cultural, and historical aspects. The process of multilateral internal consultations to develop medium-term strategies or action plans has gotten under way. Progress has also been made in bolstering commitment to development programs not only by central governments but also by subnational governments, parliaments, the private sector, various organizations and groups of civil society.

One of the main principles of the CDF is a strategic partnership among international donors, as well as a partnership between the donor community and the recipient country. In this connection we welcome the recent strengthening of the World Bank's cooperation with the International Monetary Fund, regional development banks and bilateral donors. A specific illustration of this is that the Consultative Group meetings of donor countries and organizations held under the World Bank's aegis have become more open. Their range of participants has broadened, and the participants have grown more active in elaborating and adopting decisions to enhance the effectiveness of international assistance to the developing countries. At the same time, practice shows that cooperation and coordination of donors' efforts in many developing countries, including the CDF pilot countries, are still far from perfect. We support the idea that harmonizing policies and procedures used by various donors could significantly help to improve the situation.

It is still too early to say whether the CDF is a success or a failure. Even those few countries which were the first to participate in this experiment have made only the initial steps in this direction. A much more challenging and lengthy stage is still ahead. In fact, the CDF can be judged only in terms of the extent to which it contributes to achieving development goals, that are goals of the long-term nature.

Heavily Indebted Poor Countries Initiative and Poverty Reduction Strategy Papers

The Russian Federation continues to support the HIPC Initiative and believes that the results achieved to date confirm its viability, effectiveness and great importance in mitigating the difficulties caused by an excessive external debt burden. The past year has been marked by a breakthrough in the preparatory work for implementing a massive reduction in debt burden — more specifically, in formulation of individual country Poverty Reduction Strategy Papers (PRSP). These programs will go a long way in ensuring that benefits from implementing the Initiative reach all social strata in the beneficiary countries.

At the same time, we believe that the positive effect from developing country poverty reduction programs will be far greater if they are directly tied to structural reform programs and more realistically aligned with macroeconomic indicators. Despite the appeal of using savings from debt relief for poverty reduction purposes, the main contribution to poverty reduction comes from sustainable economic growth in respective country.

As for the Initiative's "Sunset Clause," we could support extending it for a year, albeit with reservations. We view the Initiative as a one-time action to reduce to a sustainable level the external debt of poor countries that pursue sound economic and social policies. Therefore it cannot be turned into a permanent mechanism for debt forgiveness. And what certainly cannot be tolerated is the situation in which decisions already made are revised because of new external shocks or worsened terms of trade for certain participants in the Initiative.

Ever since the Initiative was adopted, there has been an ongoing debate between supporters of an accelerated debt relief and those who favor adherence to rather strict track record requirements. In this debate we tend to side with those who oppose easing the overall principles and rules, including track record requirements and shortened interval between decision and completion points. We understand that it would be wrong to penalize countries that implement comprehensive and profound reforms, by prolonging the phases of the Initiative and believe that a departure from these rules is possible in exceptional cases. But we strongly object to a revision of the basic principles of the Initiative.

In the final analysis, the Initiative will yield positive results only if each and every beneficiary country is serious in adopting a reasonable macroeconomic strategy. The legalization of loopholes and softening of criteria, meanwhile, may lead to abuses and, in effect, to the loss of the limited resources allocated for HIPC funding by bilateral and multilateral donors. This is the only kind of approach that will enable us to avoid moral hazards in the global financial system.

This brings us to the issue of financing the Initiative, which continues to cause concern. First of all, the gap between the estimated costs of implementing the Initiative and the resources actually pledged by donor countries has not narrowed over the past year, it has actually even increased somewhat. In this connection we urge all the initiator countries to take a more realistic approach to this problem and implement their own decisions. In addition, we favor granting preferential treatment, within the framework of implementing the Initiative, to the creditor countries that meet HIPC criteria themselves. Also, unsolved is the problem of covering the outlays of several regional development banks for implementing the debt write-offs. All of the above concerns should compel us to look into financial consequences of our decisions more carefully if we do not want to compromise viability of the Initiative.

Bank's Financial Capacity

The Russian Federation believes that, despite the favorable financial results of the past year, ensuring the Bank's long-term financial sustainability is still high on the agenda. Capital adequacy is the most important pre-condition for the Bank's ability to fulfill its objectives of promoting development and reducing poverty. As a responsible shareholder of the Bank, we are concerned by a number of negative trends in the financial condition of the IBRD. They include the still extremely low capital adequacy ratio, as well as the decline in lending volumes, the sharp drop in disbursements and a number of others, that may lead to a decrease in the Bank's net income.

We therefore see two major problem areas: first, capital adequacy and, second, potential decrease in the Bank's net income. Under these circumstances we favor an extremely conservative approach in allocating Bank's net income for ever-rising number of new and ongoing initiatives. The situation of volatile global economic trends and continued debate on the Bank's role and objectives in a changing world calls for caution in making long-term financial commitments. We believe that net income can no longer be the source of funding for many new initiatives, since this is beginning to negatively influence Bank's financial capacity. Having said this, we are not urging the Bank to reduce its commitments to IDA and HIPC, as well as to other important initiatives, such as post-conflict support and institutional capacity building in African countries. However, we do believe that the Bank's financial capacity is dangerously close to the limit, and we cannot seriously count on this source of funds in the future without running the risk of undermining the Bank's financial sustainability as a lending institution.

In this regard we consider that strengthening Bank's capital base will be the paramount challenge in the next few years. In the absence of consensus among the shareholders on the capital increase, the only viable alternative for reaching that goal is through allocating most of future net income to reserves. The proposed strategy will definitely require considerable self-restraint and even a degree of sacrifice for a number of years, but otherwise it will be virtually impossible to sustain financial capacity of the Bank. The IBRD's Articles of Agreement are quite explicit that maintaining an adequate level of reserves is our top priority.

The International Financial Architecture and the Role of the World Bank

We greatly value the active role of the World Bank in strengthening the international financial architecture. At the same time we believe that, in order to maximize its impact, the Bank should focus its efforts in the areas where it has obvious advantages over other participants in this process and can provide concrete assistance to member countries through lending and non-lending operations. In addition, by relying on its practical experience in supporting economic reforms and institutional development in various regions of the world, the Bank is especially well placed to bring the prospective of developing and transition economies in the process of reforming the international architecture. This will lead to decisions that take more fully into account interests of all the participants in the global financial system and will help the weakest of them to make use of the potential benefits of globalization and financial integration.

The key issue here is how to provide an adequate assessment of structural vulnerabilities and the weaknesses of existing institutions and to take effective measures to mitigate and eliminate them. In this regard we support the Bank's efforts in such areas as introducing standards and codes, financial sector assessment, improving corporate governance, accounting and auditing, public debt management and enhancing the effectiveness of national social safety nets. We would also like to underscore the importance of improving the coordination of the Bank's activities in these areas with other participants in the process of reforming the international financial architecture, primarily the IMF.

One important lesson of the international financial crisis was recognizing the need for introducing **standards and codes** in the areas of financial information disclosure, regulation of lending institutions, financial markets and payments systems, corporate governance, accounting and auditing, bankruptcy regimes, protection of creditors' rights and public debt management. We see a special role for the Bank in ensuring that the new standards, the methodology for assessing compliance and the sequencing of their introduction take into account countries' actual conditions and institutional capacities as well as existing financial constraints. For example, one problem that needs solving is the excessive complexity of the proposed standards and codes, which is delaying their introduction.

It is extremely important that the Bank pay attention to whether various standards fit the conditions of a developing or transition economy. Specifically, the automatic application of sophisticated standards that are associated with highly developed economies is unlikely to yield the desired results. It would be more appropriate here to apply basic principles and international best practices rather than very specific standards, to seek a balance between taking into account the developmental peculiarities of individual countries and applying a necessary set of standards and codes. An important aspect of the problem is to meet priorities when selecting standards and to show flexibility when implementing them in individual countries, which is possible only in close cooperation with them. We should also avoid a mechanical evaluation of compliance with standards.

One important issue pertains to incentives for introducing standards. For example, in some cases the reaction of markets to a fuller disclosure of financial information by countries may be unpredictable. An approach also should be developed for countries that for a number of reasons have been unable to comply with standards: should they be penalized by restricting access to the resources of IFIs or, to the contrary, should they receive additional technical and financial assistance? The first reports on the observance of standards and codes (ROSCs) have revealed that substantial resources are required to devise standards, develop a methodology for assessing compliance, conduct such assessments and take follow-up measures to provide assistance to the countries. The costs often exceed the resources that the countries and IFIs have available today.

An important element of the Bank's operations should be an assessment of vulnerabilities in the **financial sector**. We are pleased to note a good level of cooperation between the Bretton Woods institutions under the aegis of the Financial Sector Liaison Committee. We believe this will improve the consistency and effectiveness of assistance to countries in need. Joint participation by the institutions in Financial Sector Assessment Program is of particular value in this respect. At the same time, it is important that the results of these activities contribute to improving the quality of the Bank's dialog with governments, have a practical application in the Bank's country programs and promote higher effectiveness of the Bank's operations. It is also important to ensure proper use of confidential information and to minimize the risks associated with leaks that could lead to unpredictable market reactions and negative implications for countries concerned.

We appreciate Bank efforts to improve the system of **corporate governance** in member countries, which is extremely important in terms of attracting long-term investment and developing domestic capital markets. This field is fairly new to the Bank, and we believe that at this stage the focus should be on building up a knowledge base about corporate governance in developing and transition economies and on conducting a diagnostic assessment of the current situation in this area. On the whole, we support the use of the Principles of Corporate Governance drawn up by OECD, as a methodological basis for these activities. At the same time, we oppose the mechanical application of corporate governance principles designed for industrial countries to developing countries. We believe that the Bank should provide assistance to countries in introducing standards of corporate governance that meet basic international requirements but also take into account specific local conditions and political economy. We believe that holding planned forums on these issues in various regions of the world will contribute to this.

We support the Bank's efforts to improve **accounting and auditing** in member countries. This is of great practical importance not only for developing the groundwork for a modern market economy and financial stability, but also in terms of increasing the effectiveness of the fight against corruption. The Bank's participation in elaborating and introducing basic foundations of **effective insolvency regimes** is of particular importance for strengthening financial systems and financial crisis prevention and resolution. At the same time, we should keep in mind that this problem, which is extremely complex in the developed countries, assumes additional dimensions in a developing economy. Specifically, we are referring to the systemic effects of bankruptcies in a developing economy, the consequences of bankruptcies of state enterprises and banks, and the opportunities for abuses in this area. We believe the Bank will make full use of existing positive and negative experience on this issue and utilize the local expertise.

The promotion of **effective public debt management** is an area in which the Bank can directly contribute to reducing systemic risks in the international financial system. We welcome the Guidelines for Public Debt Management elaborated jointly with the IMF as well as Practitioner's Manual. At the same time, given the complexity of the problem, the variety of needs and the limited institutional and financial capabilities in many countries, we hope that the Bank will show flexibility in planning technical assistance programs in this area.

The events of the recent financial crisis showed that effective **social safety nets** could substantially reduce systemic social risks and promote a speedy recovery from crisis. At the same time, the social aspects of stabilization programs approved and supported by the Fund and the Bank, especially in middle-income countries, seem to be the most difficult problem, which has yet to find an adequate solution. In addition, countries that are experiencing difficulty servicing foreign debt have a serious problem in borrowing funds at market rates for supporting social safety nets. In this connection, a softening of the financial terms on the Bank's loans for these purposes merits attention.

In assessing the Bank's activities for strengthening the international financial architecture as a whole, we believe that their effectiveness will be determined in large part by the availability of appropriate budget resources, which are necessary to maintain an adequate capacity in this area. In particular, providing a sufficient number of highly qualified specialists in all of the above-mentioned areas is of great importance. In this regard we are concerned about the possible negative impact of the reduction in the administrative budget.

Finally, the Bank would make a direct contribution to strengthening the financial architecture by **strengthening its financial capacity,** and also by **refining its financial instruments set,** so that it can better provide the necessary support for countries that are threatened by a crisis or have been hit by one.

The above problems cannot be solved overnight. It will take quite some time to study them further and discuss in detail. Many of them, in our view, will shape the agenda of future sessions of the Development Committee. This will make its role and contribution more relevant in shaping a modern understanding by Bretton Woods institutions of the challenges of development and poverty eradication. In this regard the Russian delegation whole-heartedly welcomes the recent agreement between the President of the IBRD and the Managing Director of the IMF on cooperation and the joint responsibilities of both institutions.