

The Tragedy of Poverty Relief

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Mr. Chairman, Senators, I am very pleased to have an opportunity to discuss the operations of the World Bank and the need for reform of the Bank and development programs. The Commission that I chaired learned a great deal about the Bank in the limited time we had available, thanks in part to the assistance and cooperation of President Wolfensohn and many Bank staff. We are very grateful to them for their help, guidance, and information.

It is an understatement to say that the Commission was disappointed in the Bank's performance. We recognize that reducing poverty, alleviating misery, and reforming institutions is not, will never be, easy. The level of the Bank's achievements, however, is poor, much worse than the Bank's statements would suggest.

The Bank is a costly enterprise. In 1999, exclusive of the International Finance Corporation and MIGA, the Bank required \$135 billion of paid-in capital, more than \$100 billion of callable capital, and almost 10,000 staff to disburse less than \$25 billion in loans and grants. The Bank's operating cost was \$1.4 billion, more than 5½ cents per dollar disbursed to its client countries and almost \$5 million per project approved.

The Bank promotes the idea that its costs are high because its grants and loans go to poor countries with weak institutions. Some do. But 70% of the Bank's loans have gone to middle income countries that borrow in the capital markets, like Argentina, Mexico, China, and Brazil.

Poor countries, without access to the capital markets, get only a small share of the resources that the Bank distributes. The Bank has been reluctant to change its allocation toward the poorest countries. As you know from discussions of HIPC debt relief, many of these loans are not repaid. I am sure that you are also aware that corruption and misuse of funds is a constant problem. Although President Wolfensohn has made public statements about these problems, the problems remain.

Effectiveness is an additional problem. The Bank works in too many sectors and too many countries. Many of these countries could, and should, rely on their own resources or the capital markets, with the Bank providing technical assistance.

No one can be very certain about the Bank's achievements and failures. The Bank does not regularly assess the sustainability of its projects or monitor outcomes five or ten years after completing disbursement of funds. When the Commission asked President Wolfensohn why they failed to do so, he replied:

"I've asked the same questions. ...Why do we measure the data from the date of the last payment [loan disbursement]? Why do we do historic reviews of projects instead of current reviews, so that we can make sure that if we're screwing up that we can fix it before waiting seven years to see whether we got it wrong? We are also trying to look at the question of sustainability. I have no quarrel with your questions on these subjects, nor indeed the focus of your questions."

But the Bank continues to report performance at the time of last disbursement. This is usually several years before projects are completed. Under its current system, the Bank does not

ascertain whether projects are completed. If the last disbursements are stolen or misappropriated, the performance records may not show it.

Congress could take an important step forward by requiring the Bank, and the other development banks, to authorize a performance audit, by an independent auditor, of the successful sustainability and achievements of the Bank's programs three to five years after the last disbursement.

The Commission made three main recommendations designed to reduce corruption, increase efficiency, and improve effectiveness. First, the Bank should devote more resources to finance provision of global, public goods. These include disease prevention, improvement of tropical agriculture, and rational environmental policies. Second, the development banks should offer grants to improve the quality of life especially in very poor countries with corrupt regimes. In the poorest countries, the grants would cover most of the costs. Governments would not handle the money. The projects would be carried out by contractors who would be paid directly, after an independent audit certified that the results had been completed. Third, the Commission proposed an incentive-based system for structural reform that rewarded countries for adopting and continuing the legal and free market reforms that encourage, support, and sustain economic and social development.

The Commission also recommended that the Bank's activities should not overlap with the IMF. The Bank should be engaged in poverty alleviation and development finance, leaving crisis lending to the IMF. Also, the Bank should avoid overlap with the other development

banks. It should provide technical services and support to the development banks but limit its lending to Africa and regions where the development banks do not operate.

The Bank's response to these proposals has been defensive, discouraging, and disingenuous. It has claimed success rates in its programs of 80 to 93%, a bogus claim achieved by giving disproportional weight to large projects in richer countries and ignoring its own estimates of sustainability (projected at the time of last loan disbursement). The reported success rate for all projects has remained less than 50% based on the Bank's data. The Bank claims that eliminating loans to middle-income countries would reduce funding for poorer countries. This is false. The Bank lends to countries at a rate that is ½% above its borrowing cost, a margin set to cover administrative expense. The Bank claims that the substitution of grants for loans would require large infusions of new money. Dr. Lerrick has shown that, not only is this claim false, the Bank would have more resources available if it shifted to subsidized grants. And the grants program would be more effective and less subject to corruption. The Bank claims that middle-income countries would default on their outstanding loans, if they were cut off from additional Bank lending. This claim is astounding. Countries that defaulted on Bank loans would lose access to the much larger resources obtained from the capital markets.

Mr. Chairman, Senators, I regret to say that the Bank seems more concerned about its public relations image than its efficiency and effectiveness. We have shown ways to improve their practices and performance. The Bank has shown no interest.

Reform is needed to improve the quality of life and the living standards for the poorest in the world. This alone should encourage the Congress, the administration, and other governments

to insist upon improvements in the Bank's operations. Our finding that effectiveness can be increased, corruption reduced and programs expanded under our recommendations means that both US taxpayers and the citizens of the poorest countries would benefit from the proposed reforms.