Board Meeting of January 15, 1998
Statement by Khalid Alyahya

India: Country Assistance Strategy and
Haryana Power Sector Restructuring Project (APL)

The opportunity to review a full CAS for one of the Bank's most important clients is always welcome. As recent discussion in the informal CODE Subcommittee confirmed, this year's CAS for India is a significant and in many respects a landmark document, given the changed and indeed ambitious nature of the proposed three-year lending program.

Macroeconomic Developments:

It is encouraging to read in paragraph 6 that almost all the macroeconomic indicators are better than projected in the 1995 CAS. Particularly noteworthy is the sustained and impressive growth rate of GDP following the stabilization crisis at the start of this decade. This is essential for a low-income economy such as India, which still contains the largest number of poor people in the world, and with many more uncomfortably close to the poverty line who could fall below it if economic growth were to falter. Other points worth noting include the encouraging growth of exports since 1995 and the increased contribution of private investment. All of this follows from the ongoing structural reforms in investment, trade and finance. For their persistence at a measured pace with the challenging reform process successive Indian authorities again deserve commendation. In today's global environment, it is in everyone's interest that this significant economy continues to move forward and capture its considerable potential.

Having noted the progress made, it is also essential to recognize the considerable remaining challenges, of which the Indian authorities are of course well aware. High priority needs to be given to tackling the persistent public sector deficit, especially at the state level, without further postponement of needed public investment, as well as to improving the regulatory environment and deepening reforms in public sector enterprises and in the public banks. Such reforms have to be carried out in a complex political and constitutional environment, with the states moving at different paces, while maintaining the overall momentum needed to improve social development indicators.

Of course, a supportive external environment will facilitate this process, and a weakened external environment could threaten it. There is a brief consideration of the
downside risks in paragraphs 15-20, but in the light of the current Asian crisis, further elaboration or tentative updating by staff would be appreciated, especially as regards competitive and other pressures on Indian exports, and how they might affect the projections shown in Table 3 and in Annex 8. On the other hand the encouraging showing so far by foreign direct investment, the conservatism regarding reversibility of portfolio investments, and the limited exposure to short-term obligations, all offer some grounds for reassurance in the Indian case.

Some Lessons of Experience:

The discussion in paragraphs 24-28 is frank and informative, but there are two issues which in our view deserve special attention as this Chair had flagged them when reviewing the 1995 CAS. The first issue is the effect of the 15 percent cut in the Bank’s Indian program administrative budget over FY95-97 which is noted in paragraph 26, and which, in retrospect, seems to have had an unfortunate effect on project pipeline development which was not adequately foreseen at the time. However, paragraph 70 indicates that lessons have been learned from this experience, and that the Bank’s response capacity has now been enhanced under the Strategic Compact.

The second issue is the regrettable collapse in infrastructure lending, for which high if not excessive hopes were held in 1995, and the related lack of activity in the urban sector, which was expected by now to have witnessed a comprehensive process of urban reform. Some comfort is given in that the welcome process of national consultation mentioned in paragraph 23 of the present CAS specifically criticized the Bank for its withdrawal from the urban sector and for its limited involvement in addressing infrastructure bottlenecks, and that the Bank is now prepared to respond accordingly.

The Proposed Strategy:

Turning now to the proposed strategy, we note and welcome the recognition that the Bank, even if it is India’s major external development partner, must be selective (implying trade-offs) and be complemented by the work of others. The references to other assistance in the last column of the Program Matrix in Annex 1, though rather cryptic and silent as to the relative weights of assistance, are nonetheless a step in the right direction.

We have some selective comments on the strategic dimensions suggested in Section E of the CAS, followed by some general remarks on the volume of support and the IBRD/IDA composition.

On the proposed greater focus on lending to states, we note this represents a radical shift, inasmuch as the proportion of central lending will fall from 61 percent to 27 percent, while on-lending to states will rise to 73 percent, of commitments. Further, it is suggested in the Executive Summary of the CAS that this selectivity may lead to an end of lending in states where commitment to reform does not exist. However, in Annex 1 it is noted that in non-reforming states where the incidence of poverty is high, and project implementation satisfactory, some pilot activities could continue. Given the poverty burden in many states, and the Bank’s overarching objective of poverty reduction, this appears appropriate and some flexibility will be needed in this regard. Overall, a consensus-building approach, with less stress on “trying to impose conditions on reluctant clients” as paragraph 30 puts it, may well
reap better dividends in terms of development outcomes over the long term. There are also some downside risks as identified in the document, including the potential for over-concentration and possible policy reversals given the relatively short electoral cycles. Use of the new adaptable program loans (APLs) may mitigate some of these risks, but the overall situation will need careful monitoring over the next three years.

On the substantive areas for policy reform, the focus on rural development, power, and the re-entry to the urban sector are appropriate in light of poverty reduction objectives and the need to facilitate broad-based growth. The challenges nonetheless remain formidable. On the related subject of primary health and education the renewed emphasis is especially welcome. Noting the proposed involvement of IFC in the private provision of social services as mentioned at the end of paragraph 56, we wonder if there is an opportunity for IFC involvement in the education sector as well as in health care. Some comments from IFC would be appreciated on this point.

On the environment, the focus on poverty-environment local linkages is welcome. However, the third bullet in paragraph 51 which attempts to address global issues in a few words is confusing and unlikely to fully satisfy anyone. Nonetheless, the statement that the social costs of local air pollution outweigh any global environmental costs is compelling. We remain of the view that well-chosen efforts to address local environmental issues are more likely to attract consensus at this Board than are perhaps premature attempts to introduce global themes.

On the focus on private and financial sector development events in Asia have amply demonstrated the need for sustainable long-term private investment flows and appropriate linkages to capital markets and an efficient financial sector. It is to be hoped that the plans for an engagement by all members of the Bank Group according to their comparative advantages can indeed be brought to fruition in the specific Indian context.

Finally on the CAS, on the volume and composition of the proposed lending program our reaction is that this is indeed ambitious, given the anticipated more than doubling of IBRD commitments in FY98. This of course has creditworthiness implications as recognized in the document. The holding of IDA funding at a relatively constant level, somewhat below that of earlier years, indeed indicates a hardening of blend terms. It must be recalled that the performance of India's IDA projects has been above average in all respects, according to OED. In our view, this situation will underline the need for scarce IDA resources in the coming years to be used where they will have maximum general impact for poverty reduction, and not to be used for experimental purposes -- certainly not as in the past for "gap-filling" exercises related to the Global Environment Facility.

Overall, however, a key factor is that the program responds to the Government's request for increased assistance to support its development strategy of accelerated growth with equity, and we can support it. Though careful monitoring and some flexibility will be required in this new environment, we hope that the objectives of the Base Case scenario can be achieved, if not exceeded. We wish all concerned well in successfully implementing a new and cooperative strategy designed to take India into the new millennium.
Harjana Power Sector Restructuring Project - Proposed Adaptable Program Loan (APL):

We welcome this new instrument, and pleased that the procedures adopted for subsequent "follow-on" APLs are in line with those we and others had suggested when the initial proposals were presented to CODE.

We also welcome the specific application of this loan to address infrastructural bottlenecks in the power sector, which is fully in line with CAS objectives. The challenges of doing this should not, of course, be underestimated but we are prepared to give this first APL a chance to prove itself. Some of the issues involved were noted in the informative Technical Briefing held earlier this week. We would just like to stress that in our view the contribution of OED's independent evaluation of this and the follow-on loans under existing procedures will offer a good opportunity to feed back lessons of experience into subsequent activities.