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RECOVERY IN THE DEVELOPING WORLD

The London Symposium on The World Bank's Role

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Recovery in the Developing World

The London Symposium on the World Bank's Role

The World Bank
Washington, D.C., U.S.A.

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Foreword

The global economic turmoil of recent years has affected developing countries with particular severity, and attention has been increasingly on efforts to foster economic progress in those countries. The World Bank has faced new challenges as it has responded to the needs of its member countries in this difficult economic environment, and its policies have been subjected to intense scrutiny both within and outside the institution.

With this in mind, the World Bank brought together in the United Kingdom on February 14 and 15, 1985, over a hundred experts on development issues—including critics of the Bank's work—to make a candid assessment of the Bank's activities, its effectiveness, and its future directions. Among the participants in the two days of discussions were members of Parliament, government officials, representatives of nongovernmental organizations, and academics. The meeting was organized by Tim Cullen of the Information and Public Affairs Unit of the European Office of the World Bank and benefited from the expertise of an independent chairman, Professor Mike Faber, director of the Institute of Development Studies at the University of Sussex.

The symposium provided many insights into how the Bank is perceived in informed and influential circles. The views expressed have been disseminated at the Bank, and the hope is that they will contribute to improvements in the Bank's activities.

The discussions that followed the formal presentations were frank, and the remarks are not attributed to individuals. Although the discussions did not resolve differences of opinion, they allowed a serious debate to be held in a nonconfrontational setting and enabled all sides to acquire a better understanding of the complexities and difficulties involved.

JOSE BOTAFOGO GONCALVES
Vice President, External Relations
The World Bank

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Opening Remarks by the Chairman

Mike Faber
Director, Institute of Development Studies, University of Sussex

The title of this symposium, "Recovery in the Developing World: The World Bank's Role," accurately defines its main objective, but there are three other purposes I should like to draw attention to.

One of our High Street banks describes itself as the listening bank. This is not just public relations. A second purpose of this meeting is to afford officers within the World Bank an unusual opportunity—or at least an opportunity of an unusually open kind—to hear the views of some of the Bank's critics. In that respect this symposium is something of a novelty and an experiment, and its success or failure, plus the substance of what is said, will be looked at closely in Washington. I am told there has been an attempt to provide an equal platform for critical commentators of both—or perhaps I should say of all—persuasions. This reminds me of a remark that Iain Macleod once made when he was trying to fashion a constitution for Northern Rhodesia. He said that he did not expect praise for his efforts, but he hoped to achieve parity of abuse.

A third purpose of this meeting is that the officers of the Bank want us to listen to them. They want the chance to respond to our comments, to answer our criticisms, to explain and justify their current policies. Like the other institutions created at Bretton Woods, the World Bank is forty years old this year. Given its achievements, and given its immense impact on the economies of so much of the developing world, no one is likely to claim that this is a case of life starting at forty. Nevertheless, a number of factors in the world situation do mean that the Bank and its staff are confronting some major new problems that may—some in this room, I think, will argue that do—call for new types of policies. As a dealer in debt, on both sides of the balance sheet, the World Bank cannot help but be hugely concerned with the problems of developing-country debt. The collapse or near collapse of so many economies in Sub-Saharan Africa is another major concern and words like "structural adjustment" and "conditionality" are acquiring much greater importance.

The fourth purpose of this symposium is not listed in my chairman's brief, but let me put it this way. I believe that if, as a result of a clearer understanding of the Bank's policies and a better appreciation of the Bank's attitude, there were to develop among you—that is to say, among influential opinion-formers and policymakers within the United Kingdom—a greater measure of support for the Bank and its activities, that, too, would be considered a welcome result by those who have invited us to confer here.

I have been asked to chair the sessions in a manner that will encourage lively and—if I may borrow Stanley Please's favorite adjective—robust discussion in a nonconfrontational setting. I should like to thank Sir James Eberle for allowing Chatham House to be used for that purpose.

Challenges to the International Donor Community

Timothy Raison, P.C., M.P.
Minister for Overseas Development

SYNOPSIS. The international donor community faces two challenges: a changing world and an unchanging world. The second challenge refers to problems—hunger in some areas, for example—that have not responded to efforts extending over several decades. Especially for the poorest countries, official bilateral and multilateral aid are important as complements to other types of resource flows. A new, more flexible approach to official aid is needed. For several reasons, the United Kingdom intends to associate itself indirectly with the World Bank's Special Facility for Africa rather than make a direct financial contribution to it. Renewed growth in all debtor countries is needed, as is intensified collaboration between the World Bank and the International Monetary Fund in diagnosing the problems of and giving complementary advice to the developing countries. The developed countries must pursue their efforts to attain sustainable economic growth, resist protectionism, and maintain the dialogue with the developing countries.

The question I want to take up today is, how can the international donor community respond to the two major challenges it faces? The first is the challenge of a changing world. The second, perhaps paradoxically, is the challenge of an unchanging world.

Let me start with what is unchanging. What I mean is those parts of the world where, in spite of our efforts over the past three or four decades, the problems have obstinately refused to respond to treatment.

First, the problem of starvation, particularly among children, is with us as acutely as it was in the early 1970s at the World Food Conference, where we vowed to eliminate hunger. The year 1984 will be remembered by all of us for the terrible human suffering brought about by drought and neglect in many parts of Africa, particularly in Ethiopia. Some will recall the same sort of thing happening only a decade ago, and the irony is that the previous tragedy in Ethiopia resulted in a violent change of government there, and that the successor government's policies undoubtedly contributed in some ways to the current and infinitely worse situation.

But 1984 will also be remembered—and we can take heart from this—for the magnificent voluntary response by the British people once the news of the famine burst upon their television screens. Theirs was a spontaneous humanitarian gesture from one group of human beings to another. And, of course, this happened in other countries as well as in the United Kingdom.

But the problems of famine and drought are not confined to Ethiopia. They exist in many other countries in Africa and elsewhere in the world.

There are many causes of famine; drought, civil war, and population growth are among the most important. But governments' economic policies, especially in Africa, have also exacerbated the difficulties faced by Sub-Saharan Africa.

As many African governments have themselves recognized, major changes are needed in policies and management if prospects for growth are to improve. These changes are closely related to each other. The principal changes are that farmers should get a new deal, that public sector management should be improved, and that public expenditure plans should be reordered to give greater emphasis to the maintenance and use of existing assets.

In the past farmers have been given too little incentive either to export primary products or to produce for the domestic market. Governments' reluctance to pursue realistic exchange rates has adversely affected the production of cash crops. Too often, governments have followed policies of providing cheap food for urban consumers at the expense of the farmer. Reforms are also often required in the system of buying, storing, and marketing agricultural supplies. Too frequently this has been entrusted to grossly inefficient state-sponsored bodies whose costs have eaten up much of the cash needed to support basic services like education and health that can only be funded from state budgets.

The institutional weaknesses of the public sector are also related to public expenditure priorities. Too much attention has been given in the past to building new infrastructure and buying new equipment, and too little has been provided for maintenance. As a result, as I have seen, roads rapidly fall into disrepair, and buses lie by the roadside for want of spare parts and trained mechanics.

It has to be said, in fairness, that many of the glossy new projects have been sold heavily by Western businessmen. They have also often been bought on commercial credit and not with official aid. Some, nevertheless, have argued that the fault lies with aid and that all official aid is useless. They have pointed to the examples of Singapore and Taiwan to show that the economies that have made the most progress since the war have been those that have received the least official aid.

I do not agree. That is not to say that I do not recognize the importance of direct private investment and of continuing flows of commercial credit to developing countries. They have an essential role to play which aid can never conceivably supplant. But government-to-government aid also has a major contribution to make, especially in the poorest countries, which are least able to attract commercial funds, particularly for large infrastructure projects like roads, and which can least afford to service those loans. Without substantial aid, these countries could not now tackle the enormous problems they face or hope to raise the living standards of the bulk of the people to a more acceptable level in the foreseeable future. It is, therefore, to the poorest countries that Britain directs most of its aid. This is an important consideration when we are providing aid through multilateral agencies, and it is the single most important criterion we take into account when we are considering the distribution of our bilateral aid program. In 1983 about 80 percent of our bilateral aid went to countries with a per capita income of less than $800. And of course this aid takes the form of grants, not loans.

It is clear that official aid cannot take exactly the same role as it has in the past. We have all become only too conscious of the dangers of large-scale projects which require enormous sums to maintain and which may rapidly become white elephants or, in Edgard Pisani's phrase, "cathedrals in the desert." In some cases donors have perhaps been ready to fall in too uncritically with the wishes of the recipient countries, although the other extreme of trying to impose aid in ways that are not wanted is equally unacceptable. We hope we have learned these lessons. What, then, is the essence of the new approach?

We need to move away from isolated projects and to offer aid on a more flexible, sectoral basis. This provides the foundation for an effective dialogue with recipients at a sectoral level and for linking financial assistance with our technical cooperation effort.

Experience has made it clear that we must seek a closer understanding with recipients on the right policies to be pursued in key economic sectors. Then we must try to design our aid to make a maximum contribution to the realization of the recipients' policy objectives.

It also follows from this approach that better coordination among donors is vital. Donors are providing more aid in support of structural adjustment and reform programs undertaken by developing countries with assistance from the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBRD). These programs often require hard decisions by developing countries, but the donor community is, I believe, very willing to help them. Again, this reinforces the need for close coordination by all parties. Britain has long played an active role in trying to improve coordination. New arrangements have been set up in many places, most recently in Kenya, Uganda, and Zambia.

In 1983 the Overseas Development Administration (ODA) [of the United Kingdom] undertook a major review of the people for whom we are paying to work abroad. Clearly, poor countries lack many of the skills, both technical and managerial, that are required for development. For years Britain has provided the services of U.K. personnel overseas, but their numbers have declined, in some cases very rapidly. But it is clear that lack of skills and serious institutional weaknesses remain a serious constraint on economic and social progress in many African countries today. I have decided that we should be ready to give more manpower assistance to tackle these specific problems.

This is not, however, to be measured just in terms of more British people or firms working overseas. Far more important are steps to help each country improve its own management of manpower, especially in the public service, and to make its own training policy and institutions more effective. This means that we too need on our side a more systematic approach that will focus on the objectives and needs of particular institutions, that will further integrate the supply of personnel within our training programs, and that will relate to the labor market, the manpower policies, and the educational developments within the country.

I should add that changing the emphasis of our policies does not mean that we have to change the fundamental characteristics of what I believe to be the best donor agencies. These characteristics are a conviction that we are doing the right thing, dedication to see the tasks through, and a sound professional approach to what needs to be done. These qualities are certainly evident in the World Bank. I like to think, too, that they are to be found in ODA. So there is a close identity, not only of ideas but also of attitude, which has made possible the long and effective cooperation between successive British governments and the World Bank.

This is why, at a time when our funds are short, we believe that association of our bilateral aid with that of the World Bank is the best way we can play our part in the Bank's Special Facility for Sub-Saharan Africa, since we cannot make a direct financial contribution. A direct contribution from the United Kingdom to the Special Facility could only be made at the expense of our bilateral aid, including that to African countries, and both the secretary of state for foreign and Commonwealth affairs and I know, as a result of our recent visits to Africa, that this would be far from welcome. Of course, it would be most welcome if we could both maintain our bilateral programs and make a contribution to the Special Facility, but since we cannot, robbing Peter to pay Paul does not seem to be a sensible solution.

It is argued that since the supplementary fund for the seventh replenishment of International Development Association (IDA) resources has not come into being, the cash we had for that must still be available for the Special Facility. Life is not, unfortunately, as simple as that. Since January 1984 we have agreed to contribute to the European Development Fund (EDF), which is considerably larger than had originally been envisaged. Let me remind you here that the bulk, probably 90 percent, of this fund, worth £4.4 billion, of which the U.K. share is around £700 million, will go to Sub-Saharan Africa. And, of course, we are determined that the EDF, under the next Lomé Convention, should be an increasingly effective aid organization.

Against that background, when we attended the donors' meeting to discuss the Special Facility in Paris in January 1985, we proposed to play our part in the World Bank's initiative indirectly instead of by making a direct financial contribution. We are doing this by earmarking, for use in close support of the Special Facility, disbursement of £15 million a year of bilateral aid in each of the five years during which it is expected that the Special Facility will disburse funds. Our money would be made available on grant terms, and it would be subject to the same conditionality as the World Bank funds. I believe that those proposals represent a real contribution to the success of the Special Facility.

Let me now turn to the challenge of the changing world. The problem that has been at the top of all our preoccupations over the past two or three years has been the developing countries' debt. The problem is still with us. Although there is an encouraging recovery in the world economy and no longer the same sense of immediate crisis, formidable difficulties remain. Because of the massive amounts involved and the potential risks to the international financial system, attention has in the past been focused on the major Latin American debtors. The problem is no less severe, however, for the poorer countries. The challenge facing us is to secure renewed growth in all the debtor countries, and there is no one global answer. Progress thus far demonstrates that the case-by-case strategy remains valid—indeed, essential.

All of us have had to adapt our policies to meet these challenges. Here I would pay tribute to those developing countries which have taken the necessary, and often very painful, measures of adjustment. The World Bank, too, has responded swiftly, becoming more flexible in its lending instruments and in tailoring development programs to individual circumstances.

We regard the Bank as being in the forefront of the efforts to bring about the necessary policy reforms—the cutting edge in this delicate but vital area of multilateral and bilateral aid efforts. The raison d'être of the Bank is not, however, to address the problems of a country's indebtedness; that is the responsibility of the International Monetary Fund. But where IMF assistance is sought by borrowers from the Bank, it is clearly important that the two Bretton Woods institutions should collaborate closely to see that their diagnosis of the underlying immediate and medium-term problems is broadly the same and to ensure that their advice and recommendations are complementary. I pick two areas where this complementarity is typically needed.

The Fund sometimes finds a need for exchange rate adjustment, which the Bank sees as a prerequisite to aid for the revival of agricultural or domestic production. And the Bank's concern with restructuring the balance of public investment programs and the links between these and government recurrent spending has obvious links with the Fund's attitude toward borrowing limits.

The Bank can play a direct part in the short term by helping through some balance of payments support in its structural adjustment or sectoral lending. But it is important that such lending be directly related to the required reforms. We realize that borrowers may sometimes not wish to borrow from the Bank on such terms. We must accept this, but we would not expect the Bank to dilute its recommendations about the reforms which it believes the would-be borrower should carry out.

As you would expect, the Bank has been quick to look at the implications for its own role in the changing world. It will be putting forward proposals at the meetings of the Development Committee in April. Member governments will look at these closely with the Bank's management. I do not want to say any more about it now, except that I doubt that either the Bank management or the United Kingdom will make any radical proposals for change.

I should perhaps mention here a particular issue which has struck us recently. There is, we believe, a need for the Bank to give a signal to borrowers that it is reviewing critically the growth in its own staff numbers and administrative costs, which have expanded considerably over the past years. I say this because such increases have come at a time when many member governments, including our own, have been obliged to effect their own severe adjustment policies, which include a strict containment of public spending. And such action has, of course, been urged on many developing-country borrowers by both the IMF and the World Bank.

But this is a minor point when set against the Bank's achievements. Among them I should perhaps single out one of the major innovations, carried out under Mr. Clausen's leadership, which is one for which the Bank's borrowers can be most grateful. This is the introduction of the variable lending policy. Since IBRD adopted the policy of variable rates, the rate of interest for loans to developing countries has fallen from 11.43 percent to its present rate of 9.29 percent. The Bank's achievement, which is a tribute to its borrowing and investment policies, is all the more remarkable since it has taken place when market interest rates have been generally high, as we all know only too well.

However effective the Bank and the Fund are, they cannot act on their own, and it is very important that the developed countries should play their part. Doubtless the single most important contribution we can make is to secure noninflationary, sustainable growth and to ensure that the benefits are spread to the developing countries.

We must continue to resist, and where possible roll back, measures of protection. Lower interest rates and a lower dollar exchange rate would obviously help greatly.

At the London Economic Summit, finance ministers were asked to consider the scope for intensified discussion of international financial issues of particular concern to the developing countries. As a result, the dialogue between the developed and developing countries continues at the spring meetings of the Interim and Development Committees. We hope these meetings will build on the progress already made. We will continue to work with the developing countries, within the framework of the competent international institutions, to find practical solutions that have a real chance of success. Multiyear rescheduling arrangements and resumed export credit cover in the context of successful implementation of programs of adjustment have already been considered. Short-term bank lending on the same scale is neither likely nor desirable, and we must now look carefully at ways of securing more stable long-term finance for the developing countries.

Let me conclude by expressing the hope that your discussion over these two days will be stimulating and useful. Your symposium is being held at a difficult time, when the economic difficulties of Sub-Saharan Africa and the apparently constant problem of international indebtedness are encouraging us all, developed and developing countries alike, to look afresh at the way aid passes from the rich world to the poor. The spring meeting of the Development Committee will provide the immediate focus for this dialogue, but we cannot expect that it will provide all the answers. You, in your discussions here today and tomorrow, have the opportunity of feeding in ideas which could prove helpful. I am sure that you will seize this chance, and I look forward to hearing and seeing the results of your work.

Discussion

The comments centered on the United Kingdom's policies on and financial contributions to official development assistance. Some concern was expressed that the percentage of the United Kingdom's gross national product (GNP) being allocated to such official aid was not only not being maintained or increased, as recommended in the London Summit communiqué, but was actually being reduced. In response, Mr. Raison referred to the priority being given by the present U.K. government to the control of all areas of public expenditure, including the aid program. Although the United Kingdom had not attained the target of 0.7 percent of GNP for official development assistance, the British aid effort was deemed to be having a considerable impact overall and was held in high regard as a well-run program.

A comment was made about the extent to which bilateral aid, as distinct from multilateral aid channeled through the World Bank, was increasingly being spent on backing up business deals with developing countries. The practice often led to expenditure on capital equipment that was then left to decay and go to waste.

Mr. Raison conceded that the United Kingdom's bilateral aid was substantially tied to the procurement of British goods and services, but he added that it was a mistake to perceive the entire aid program as becoming purely a vehicle for promoting British exports. Incentives being provided by the government to private investment overseas included the removal of exchange controls as well as the successful negotiation of investment protection agreements with about twenty countries to date.

The degree of fungibility in public resources was discussed in the context of the United Kingdom's decision to provide bilateral aid in parallel with the Bank's Special Facility for Sub-Saharan Africa rather than directly to it. It was thought illogical to justify Britain's indirect participation in the facility on the grounds that the new Lomé agreement would absorb the money that would otherwise have been available to the Special Facility. The exact status of the money that would have been allocated to a fund to supplement the shortfall in the seventh IDA replenishment was also questioned.

Mr. Raison explained that one neither could nor should assume that a sum of money originally intended to be available for one purpose, such as allocation to the IDA supplementary fund, could easily be transferred to another purpose. Indeed, it was not possible to say precisely how the aid budget would ultimately be spent beyond the public expenditure triennium. As for the apparent discrepancy, mentioned by a speaker, between the three-year term of the Bank's Special Facility and the commitment of British bilateral aid in parallel for a five-year period, disbursements from the facility were expected to occur over five years. Whether the United Kingdom's parallel contribution would be on the same untied-procurement basis as German, Swiss, and Japanese joint financing had not yet been decided. [*Note*: The U.K. contribution was subsequently untied.]

The viability of official bilateral or multilateral support to land reforms that included among their objectives equity redistribution was questioned. It was noted that the question of land reform was one of the most acute political and social difficulty. The British experience with this issue in Kenya after independence had led to wariness about active involvement elsewhere. As for the Bank, its policy since 1975 had been and remained one of supporting well-conceived land reforms through assistance to governments in their planning efforts and in schemes to provide credit to farmers. Few operations had been financed by the Bank for the explicit purpose of effecting land reforms because few governments had undertaken such programs or sought assistance for them.

A question was raised concerning "the silent takeover of policymaking by the Americans, especially within the Fund but to a certain extent within the Bank." It seemed to the speaker that this had led to a series of decisions that gravely undermined the actual and prospective ability of both institutions to carry out their functions. He suggested that it might be desirable to look more discriminatingly at what the interest of the United Kingdom and the wider community might be, rather than to pursue a general policy of support for the American position. Moreover, Britain might consider taking the initiative in formulating a coherent European policy toward the Fund and the Bank and their future evolution.

The Debt Crisis and Its Impact on Middle-Income and Poor Countries

Nicholas Hope
Chief, External Debt Division, The World Bank

SYNOPSIS. The heavy indebtedness of a few developing countries has affected the international financial system and the prospects for growth of the indebtedness of developing countries as a group. The growth and transformation of debt since 1970 had led to the accumulation of a heavy debt-servicing burden by the time the recession of the early 1980s set in. In the aftermath of the mid-1982 Mexican debt crisis, the most attractive option for dealing with the global debt problem appeared to be to raise the debt-servicing capacity of the debtor developing countries. The present situation has substantially improved for the major market borrowers. Their momentum toward growth has been resumed and is projected to increase, assuming that the nations of the Organisation for Economic Co-operation and Development (OECD) can sustain annual growth rates of 3 percent. For the African countries, however, the outlook remains bleak. As for the future beyond 1985, the Bank sees reasons for some pessimism about the prospects for satisfactory management of the global debt problem.

At the end of 1984 the total gross indebtedness of the developing economies (broadly defined) had reached an estimated $895 billion. We project that by the end of the year the figure will reach something like $975 billion. The core of those estimates is the long-term debt information that 104 countries report to the World Bank under the Debtor Reporting System. For those countries, long-term debt of $600 billion at the end of 1983 rose—partly because of rescheduling of short-term obligations—to about $655 billion at the end of 1984 and will rise again to around $710 billion by the end of 1985.

There is a mind-numbing quality to these sorts of numbers, a quality that is perhaps best exemplified by a remark attributed to Everett Dirksen, when he was discussing the U.S. budget. He remarked, perhaps prophetically, "A billion here and a billion there, and pretty soon you are talking about real money." To a large extent, this is the situation with the debtor developing countries. Debt has reached levels that stagger the imagination and make it conceptually very difficult to analyze.

My mandate is to try to go beyond the numbers and say something about the way in which that debt affects the growth prospects of developing countries and in particular the prospects of two groups: the major borrowing countries—the developing countries that are the biggest borrowers in financial markets—and the very poorest countries, the problem debtors of Africa. That is an immodest undertaking, especially as I have only twenty minutes. Fortunately, experience suggests that I do not need to say much to provoke a continuing discussion of the issue. And if I can manage just to direct conversation in certain avenues, I will be happy to let the discussion take care of itself.

Let me say first that there are two key issues in the debt of developing countries. The first issue is, to what extent do the obligations of developing countries to the banking system affect the economic health of the commercial banks and the overall stability of the financial system? The second is, to what extent does the external indebtedness of developing countries inhibit their own prospects for growth and impair their chances for progress in development through the rest of this decade and beyond?

By distinguishing those two issues, you immediately split borrowing countries into two groups. First, there is the group of countries that are big enough borrowers to affect the financial markets. To my mind, the bulk of the policy considerations of the international community in the past four or five years has focused much too closely on the problems of that group. The second group—the poorer countries for which in some ways debt is a more intractable problem—is no more than a minor irritation to the financial markets. This group also had to renegotiate its debt, but the debt owed to bankers is not large enough to create substantial problems for the financial markets, and so the problems of the poorer group of countries have been comparatively neglected. For both groups of countries, however—the big market borrowers and the comparatively poor borrowers—the real issue is the effects of external debt on growth and development prospects in 1985 and beyond.

To focus the discussion, I would like to do two things. First, I would like to review briefly what has happened to debt since 1970. Then I would like to describe the current status of the developing countries' indebtedness and look to the prospects both for a resolution of their debt problems and for a strong resumption of their growth.

Debt grew very fast in the 1970s. That is not news. Everybody knows that the long-term debt of developing countries grew at over 20 percent a year for the decade. In the 1980s it has grown some 10 percentage points a year less. What that means, looking only at the long-term indebtedness of the countries we monitor, is that external debt doubled between 1970 and 1974 and then trebled by 1980, when it reached $142 billion. Since then we have had a comparative stabilization, only a 60 percent increase, to some $655 billion by the end of 1984.

The growth of debt was remarkable, but perhaps even more so was the change in its structure. The 1970s saw a strong movement to borrowing by developing countries from the private markets and on floating interest rates. There was a sharp reduction in the share of bilateral official lending and, associated with that, an equally sharp reduction in the share of developing countries' debt on concessional terms. The debt of developing countries on concessional terms was two-fifths of total debt in 1970; it is now less than one-fifth.

To me, the most striking statistic is the increase in the share of developing countries' debt that is public borrowing from the financial markets. In 1970 only 12 percent of the developing countries' debt was debt of sovereign borrowers owed to the financial markets. By 1980 that share had risen to 38 percent, and in 1983 it was 44 percent. As the rescheduling process proceeds, that trend is reinforced; increasingly, short-term and private obligations are converted into long-term obligations of the public sector, a large part of which is to the markets. So we can characterize the 1970s as the period in which the sovereign borrower discovered the financial markets or, viewed from the other side, the decade during which the banks discovered the sovereign borrower.

Why did debt grow so fast? I think the accepted explanation, and one that clearly is important, although it tends to neglect the growth in lending to developing countries from markets that began around 1968–69, is the first oil shock. It created a need for financing. The funds that the countries of the Organization of Petroleum Exporting Countries (OPEC) earned from much-increased revenues from oil sales had to be recycled, and the recycling medium was principally the commercial banking system. At the same time, the accommodating monetary policy in the United States and in most other industrial countries led to excessive levels of inflation and to low levels of real interest rates, which encouraged countries to finance substantial external deficits through recourse to the markets.

A neglected explanation of why debt grew so quickly is that the countries could borrow. Developing countries had become creditworthy, largely because their development policies had been extremely successful over the previous twenty years. By the mid-1970s many of the developing economies that were borrowing heavily in the market were very large economies in their own right. They had established an enviable record in their dealings with the markets and—given their growth rates in relation to those of the industrial countries—they looked like extremely good investment prospects to the commercial banks.

Creditworthiness was helped as well by the fact that, even though developing countries' debt grew very rapidly in the 1970s, their exports grew even faster. As a result, in 1979–81 the ratio of debt to exports actually had fallen from its value in 1970–72. So, developing countries were not borrowing without considering what they needed to do to retain creditworthiness.

There were, of course, adverse changes from the viewpoint of debt management over this period. Debt service grew very fast—faster than debt or exports. The reasons are obvious: as you borrow more from private sources at shorter maturities, and as you borrow more on floating interest rates, you pay substantially more for your loans. Also, beginning in the mid-1970s there was a secular rise in interest rates for both official and private loans. So, although the developing countries maintained a stable debt-to-export ratio, they still faced substantial increases in their debt-service ratios—the share of their exports absorbed by interest payments and amortization of principal.

The situation was such, however, that in the *World Development Report 1980* we could still take a rather sanguine view of most developing countries' debt-servicing prospects. The key issue seemed to be whether we could sustain creditor confidence; that is, would creditors continue to support countries while they implemented the economic programs that would be necessary to adjust to the oil shock of 1979? Optimism about the developing countries' ability to service what they had already borrowed did not extend to their ability to continue borrowing heavily, nor to their ability to sustain high growth rates in the early 1980s.

The prospects for debt-servicing difficulties seemed quite high if real interest rates stayed up, if the growth of developing countries' exports slowed sharply with recession, if commodity prices stagnated, and if official support for developing countries did not respond to their increasing financial needs. As we now know, in all of those areas the outcome was adverse. In 1980–83 the international economy entered the most prolonged recession of the postwar period, and that created a situation in which many developing countries began to experience increasingly severe debt-servicing problems. Except for some African countries, however, most of them managed to struggle through until August 1982 and the shock called the Mexican crisis.

For many years I tried to avoid using the term "crisis" in association with debt, largely because I think it devalues the term. We have experienced a period of severe economic difficulty that for many developing countries is now four or five years old (for industrial countries it may be a decade old), but to me the problems of external indebtedness do not necessarily justify that term. (In Washington one quickly learns that a crisis is "an event attended by a journalist.") Looking beyond emotional reactions and the staggeringly large debt numbers, if real economies had responded, there was no reason, through 1982, why debt levels should be unmanageable.

In the case of Mexico, however, given the trauma of the event and its aftermath, crisis is clearly the appropriate term. That leaves us with two questions, which I will not attempt to answer here. The first is, could the crisis have been avoided by a better mix of policies, especially if the Mexican government had taken hold of the demand management situation earlier? (Or, alternatively, if the industrial countries' policies had contributed to further growth of the international economy, could the developing countries generally have avoided the widespread problems with external debt that have shaken the confidence of the financial markets?) The second question is, could we have contained the problem of Mexico if we had had in place better institutional arrangements for restructuring external debt obligations? That is a more relevant question, perhaps, to what we expect to see in the years to come.

Well, where are we now? We have three ways of dealing with debt problems. One is to write off the debt. That is an unattractive option for all concerned—with the exception of some of the poorest African countries—and it could be extremely damaging to the major market borrowers. The biggest borrowers have worked hard to gain access to financial markets, and their longer-term economic health is crucially linked, through international trade and payments, to the financial markets. There is no way that they could accept a write-down of their liabilities without jeopardizing their future access to those markets. Most banks, anyway, see no need to write off a claim that they expect to be serviced in full.

Another way to deal with the problem is to reduce the debt outstanding to something consistent with the existing capacity to service it. To do that, developing countries have to run current account surpluses, which is undesirable at any time for those countries if they are to grow fast, but in the existing economic environment has been tantamount to impossible. Many have attempted to do so, in the sense that to improve their debt-servicing prospects they have resorted to austerity programs to compress imports and have adopted policies to promote exports.

The most attractive way of dealing with the problem is to raise the debt-servicing capacity of countries as rapidly as possible so that they can service the debt they had borrowed in the expectation that the world would be different from what it turned out to be. Three things will help developing countries raise their debt-servicing capacity: high export growth, lower real interest rates, and more official support from industrial-country governments and international agencies. We might add a critical fourth factor—creditor confidence. Creditors need to regain confidence in the developing countries' ability to service their debt because—as we were shown graphically in the case of Mexico—if you are coming to the markets to roll over large sums at a time when they are reluctant to lend you another farthing, then you are going to have extreme problems managing external debt. You can manage debt in the 1980s only by ensuring that your access to the market is unimpaired, and this means that creditors must be confident that you can pay.

For most developing countries, 1982 and 1983 were periods of attrition. They went through interminable negotiations with creditors to stabilize their financial situations. By 1984 we saw a very substantial improvement for the major market borrowers. By contrast with the previous two years, their improvement in the external accounts was generated from export growth. They managed to come to terms with creditors, by and large. In particular, we had what I regard as a watershed in international relations, the multiyear rescheduling arrangement agreed in principle for Mexico. The countries, on average, began to grow again in per capita terms for the first time in this decade, and they achieved something like a 3.5 percent growth in 1984.

The World Bank expects that growth to increase to about 4.25 percent in 1985, on the assumption that the industrial countries, although growing less rapidly than in 1984, as the U.S. economy slows, will grow at around 3 percent. The developing countries also benefited from the success of their own policies for adjustment. The biggest debtors demonstrated, consistent with the size and sophistication of their economies, an extraordinary capacity to adjust their economies under what were exceedingly harsh international conditions.

Looking to the future, I feel in a somewhat equivocal situation. In the early 1980s the Bank was regarded as being somewhat optimistic because it said that the developing countries were not going to bring down the markets. Our position was, "The problem is not that the developing countries won't service; the problem is that they won't grow, and if they don't grow, ultimately they may not be able to service their existing debt because they borrowed in expectation of rising GNPs and rising exports." Now that things seem much better, now that there is extraordinary confidence in the international financial community and in major policy agencies, both internationally and at the government level, that the international financial situation can be managed, I think the Bank is rather more pessimistic than some other borrowers about the longer-term prospects for resolving the debt situation satisfactorily.

On the assumptions that the industrial countries can achieve growth of something like 3 percent a year in the next five years, that real interest rates will fall to about 4 percent by 1990, and that exports of developing countries to the industrial markets will grow at something like 5 percent or 6 percent a year, the middle-income developing countries might expect to restore their growth to about 5 percent in the last half of the decade. That could be enough for them to resume the momentum of development that was largely arrested in the first five years of the 1980s. With growth of only 2 percent a year for the middle-income countries, we have had a pause in the development process that has been unknown since the war. To my mind, that pause has been so severe that it threatens the longer-term momentum of development and even the gains made by developing countries and the international community over the past thirty years.

For the African countries, unfortunately, even under these somewhat optimistic assumptions growth would be no more than about 3 percent a year. That would mean continuing declines in per capita income for many countries. It would mean, in fact, that for a generation of Africans in some countries the standards of living would continue to deteriorate.

What are the uncertainties in the outlook that make me less positive about 1985 and beyond than some other observers perhaps are? First, real American dollar interest rates were higher in 1984 than they have been at any time in the decade. The major uncertainty over whether interest rates can fall is the size of the U.S. government deficit; the prospects that there will be substantial alleviation of the deficit in the near term seem poor. Second, OECD growth may not be sustained at around 3 percent. Third, the dollar has stayed high for a remarkable period of time, but if it did fall abruptly, the underlying assumption of 3 percent growth could be threatened by the actions taken to stabilize exchange rates.

On the side of regularizing relations with creditors, we have made considerable progress for a couple of countries. But progress is needed for several more before we move into an economic downturn, because in a world in which countries renegotiate debt annually policymakers cannot focus their attention on the longer-term policies for structural adjustment that are still required in many major debtor economies.

Finally, as our previous session indicated, there is nothing in the outlook to suggest that official support is going to increase substantially in the last half of this decade. We have had something of a restoration of the balance between private and official financing in the first half of the 1980s, but that is by default, occurring only because private lenders have attempted to withdraw. If official lending does not increase substantially in the second part of the decade, the job of the developing countries will be much more difficult, and, without more aid, for some of the African countries it may become tantamount to impossible.

Let me close with some specific comments about Africa. I do not think you can argue that debt is the problem for Africa. If all the debt of Africa were canceled tonight, tomorrow the countries would rise to face precisely the same problems of inadequate human and physical capital and natural resources that now plague many of them. But external debt critically constrains the ability of African governments to implement the policy reforms that many of them, and I think most of us, now see as essential if they are to begin to restore some momentum to their economies. Perhaps one analogy to this current financial situation is that of a horse trying to clear Beecher's Brook without taking a run. The developing countries of Africa are oppressed by their external financial overhang. Some policymakers have suggested that the major borrowing countries ease their path to regularizing external financial relationships through their own capacity to adjust. In the African situation, by contrast, meaningful adjustment may become a realistic possibility only after a satisfactory solution to their financial difficulties is in place.

Discussion

A speaker asked whether any serious studies were under way in any forum to evaluate the potential impact on the world economy of a default by the debtor countries.

Mr. Hope replied that no such formal study was being conducted in the two Bretton Woods institutions, mainly because such studies had been and were being done elsewhere—at the Brookings Institution and the Wharton School of Economics, for example. The studies supported the conclusion that a default by a major debtor would be extraordinarily harmful to the economic prospects of that country.

In one speaker's view, default did not appear to be an option any developing country would choose to exercise, because the cost of withdrawing from the integrated international trade and payments system would be so high. Moreover, the benefits of remaining part of the system were presumed to be immense; in fact, this assumption was the very cornerstone of multilateral development assistance.

Others said that default could not be ruled out as an option, however unattractive it might be. There was reason to question whether the present treatment of the debt problem by emphasizing debt servicing through painful economic adjustments could be sustained without revolutionary political and social consequences. It was noted that a recently completed study by a *Financial Times* correspondent, sponsored by the Twentieth Century Fund, examined in a perspective of political realism the specific sanctions and incentives that might face a defaulting debtor. Its conclusion was that, because of a significant shift in the balance of power between debtors and creditors and the absence of meaningful sanctions available against a large defaulter, a debtor country might calculate that the financial gains it stood to make from a default far outweighed the costs. The philosophy of not antagonizing financial markets as long as a particular debtor had hopes of continuing to borrow from them to service debt may have made sense at the time of the Mexican crisis in 1982, but against the background of today's situation (in which Brazil, for one, would be expected to pay $12 billion in interest every year between now and the end of the century and was unlikely to be able to raise such sums from the markets on a voluntary basis), the default calculation looked very different.

A speaker suggested that it might be sensible to approach the debt problem by focusing not on servicing the debt but on repaying the principal through the sale of productive assets such as equity shares in a national oil company. Although this was deemed unattractive by the debtor governments, many of which perceived it as parting with some of the national patrimony, it could lead to an easing of the debt burden without the adoption of the belt-tightening policies advocated by the IMF to ensure debt servicing. The speaker wondered whether the international community could press debtor governments to liquidate at least part of their debt, possibly on a discounted basis, by a transfer of assets—not necessarily to the particular commercial bank to which the money was owed, but perhaps to the World Bank, by giving it productive paper as distinct from all-but-worthless government paper. In his view, such a process, involving the transfer of a tangible asset, would draw the private sector into a continual process of development.

Mr. Hope agreed that it might be possible to use equity to replace some of the debt in developing countries, particularly in light of the current level of interest rates, which made equity participation seem more attractive to some developing countries. The difficulties with this approach were in finding private direct investors who wanted to put equity into developing countries and, conversely, in ensuring that the developing countries would be getting full value for the assets they would be giving up. For example, there was no doubt that some commercial banks would gladly write off a debt in return for acquiring a network of banks in the debtor country, but most debtor nations would be reluctant to strike a deal of that sort.

On a somewhat different subject, the point was made that in 1984 some $26 billion in capital flowed from the developing countries (particularly in Latin America) to the developed ones and that, in extremely oversimplified terms, it could be said that Latin America was contributing to the financing of the U.S. deficit. Could anything be done to stop this outflow of funds or to restore new flows to counteract it?

In response, it was noted that the solution lay in enabling the debtor's servicing capacity to expand by opening markets in the industrial countries to exports from developing ones, thereby providing the latter with more export earnings with which to service their debts. The raising of the export base, in turn, depended on the resumption of growth in the global economy and of voluntary capital flows from commercial sources. The potential role of the World Bank would be to facilitate the transition from the current short-term adjustment phase, which involved a partnership between the IMF and the commercial banks, to a situation in which a durable tripartite relation among the commercial lenders, the debtor countries, and the international institutions made it possible for countries to adopt policies for long-term adjustment and growth. The Bank could help this process by assisting in the formulation and implementation of such adjustment programs. It was asserted that the Bank would indeed take into account the domestic political pressures on governments to respond to their populations' expectations of economic improvements and would not insist that all export revenues be directed solely to debt servicing if this would preclude growth.

A few speakers drew attention to what they considered to be a shift in Bank policy away from human resource development and toward privatization. They wondered whether the Bank had perhaps "lost its way" when it started to toe the IMF line more closely in its own policy advice to member countries, and whether at present the impact of the Bank on the poor was possibly more negative than positive.

In response, speakers disputed the thesis, implicit in those comments, that economic adjustment policies had to be at the expense of the poor. On the contrary, they argued, the adjustments that were essential to revitalizing a country's productive base often directly improved the lot of the poor, especially in rural areas. In their view the Bank had not abandoned its "basic needs" philosophy; rather, it was attempting to help its member countries regain some momentum toward development by discussing with them in blunt and forthright terms the realities of the situations in which they now found themselves and the nature of the actions they would have to take to improve those situations.

The World Bank—Where Now?

Stuart Holland, M.P.
Shadow Minister for Overseas Development and Cooperation

SYNOPSIS. The IMF adheres to an outdated financial orthodoxy, based on the twin pillars of deflation and devaluation, that is now seriously damaging the global economy, and it determinedly denies a mixed-economy framework for developing countries. The World Bank has failed to recognize and deal with the globe-spanning colossus of multinational capital. The Bank still argues naively that price and market distortions hinder growth and does not recognize the limits to market forces. It holds up the "four little tigers"—Hong Kong, the Republic of Korea, Singapore, and Taiwan—as examples of successful economic development on which other countries should model themselves, yet these countries have achieved economic growth not by rigorously applying the tenets of textbook market economics but by combining major state intervention in economic areas with ruthlessly repressive political and social policies. Although it is true that there is now no broadly agreed set of social, economic, and institutional criteria for promoting development, challenges to the primacy of market forces and processes as the determinants of relative growth performance are increasing. This is especially obvious in Africa, where the free working of market forces in no way enables countries to countervail the constraints of monetarism and multinational capital. The politicians of industrial countries, who are mainly responsible for the policy directions of the Fund and the Bank, must recognize that only global redistribution can ensure economic recovery, that the developing world's primary needs are for social rather than private capital accumulation, and that priority expenditures on essential programs for housing, health, education, and social services will result in sustained deficits by developing countries. Global recovery from the crisis is possible provided that industrial-country governments not only accept such sustained deficits but also reject the IMF's conditionality

and its twin-headed axe of devaluation and deflation. As for the Bank, it could in the future perhaps step out from the shadow of the Fund and become a force for global development by pressing the case for major redistribution and recovery programs.

The World Bank—where now? It is quite clear that the present global crisis is structural rather than cyclical. It reflects the end of long-term postwar reconstruction and the end of dollar hegemony. Postwar reconstruction, especially in the European and Japanese economies, was assisted by the World Bank. But the role of the Bank was insignificant in comparison with other factors, in particular the long-term rise in public spending in advanced capitalist countries and especially in Europe. Public spending (including transfer payments on social security) went from around a third to two-thirds of gross domestic product (GDP). In other words, a key role in postwar recovery was played by the rise of welfare spending and a mixed economy. Perfectly reputable models of economic growth, such as those of John Hicks, stress how long-term autonomous expenditure can prevent the market economy from sinking into a slump syndrome. Certainly, public spending played such a role in postwar recovery up to the mid-1970s in sustaining demand and preventing a major slump.

Beginning in 1975 the OECD countries overreacted to the OPEC price increases, put on the brakes rather than touching the steering or changing down a gear, and substantially caused the ensuing contraction of output. OPEC surpluses were recycled to the developing world and especially to Latin America, but the combined impact of higher energy costs and deflation undermined South-South trade, especially for countries such as Brazil, where it has been estimated that some 70 percent of manufactured exports had previously gone to other countries in the South. The debt of developing countries, depending on what you include in the measurement, is now some $800 billion—a potentially catastrophic equivalent of about a third of their combined GDP.

We have been told time and time again that the Fund is really a bank and the Bank is really a fund. But in reality, if the Bank is less than a fund, the Fund is more than a bank. It is the iron fist of an outdated financial orthodoxy that is now seriously damaging global development. The Fund's policies were never radical, since Harry White beat John Maynard Keynes at Bretton Woods. Sound money principles, backstage when the world economy was growing, came to the fore when OPEC price increases followed the devaluation of the dollar. Developed and developing countries alike were caught in the monetarist maw, including some of the Fund's own key subscribers.

Monetarism is a new name for an old game, currently identified with

Milton Friedman but dating from Locke and Hume. It entirely predates the modern capitalist state as spender, social guardian, planner, and entrepreneur. It focuses—as I think we all know—on relations between money supply and prices in Fisher's equation and ignores the velocity of circulation or the levels of transactions and demand. In the mid-1970s, Keynesians in the world's treasuries and chancellories went down like ninepins because they shared the monetarists' analysis of the inflationary gap—in essence, too much money chasing too few goods and services.

In reality, global inflation is complex and as multiple in its origins as the price mechanism itself. Clearly, increased oil prices played a central role. Yet average rates of inflation in the advanced capitalist countries had already doubled in the decade before the 1973 OPEC price increases, for both demand-pull and cost-push reasons. At the time, attention focused on cost-push from labor and big unions. But there was also price-push from big business, as leading companies compensated for falling rates of growth by raising prices to preserve their cash flows.

Friedman's associations of the growth rates of money supply and price inflation have been incisively challenged over the past decade. James Tobin in the United States, in particular, has stressed that even in the U.S. data produced by Friedman and Anne Schwartz, the master of monetarism changes his definition of money supply to suit the period and the price inflation in question. Such economic methodology is, at best, open to fundamental question. At least it is unscientific. Had Milton Friedman been playing cards rather than playing with people's jobs, such shuffling of the pack on money supply to suit the hand he held would have ensured that he was thrown out of any self-respecting casino.

Meanwhile, since the postwar settlement that established both the IMF and the World Bank—whose economic orthodoxies related to spending and trade between different companies in different countries—multinational capital had come to span the world economy like a colossus. In the early 1970s direct production by multinationals in different countries already exceeded total world trade. By 1982—as illustrated by Clairmonte and Cavanagh (1984) for the United Nations Conference on Trade and Development (UNCTAD)—the combined sales of the world's top 200 corporations exceeded £3 trillion, equivalent to nearly a third of the world's gross domestic product and one and a half times the total production of developing countries. Significantly, more than half of such corporations have their headquarters in just five countries, all of them crucial to the funding of the IMF and the World Bank—the United States, Japan, the United Kingdom, the Federal Republic of Germany, and France.

UNCTAD's 1984 figures show that between two-thirds and the whole of global trade in minerals, commodities, and food products is controlled by multinational companies: these are developing-country exports. This has cataclysmic implications for developing countries inasmuch as it is not untypical for only one-tenth of the final value of the minerals, commodities, or food concerned to accrue to producers. Only one-tenth or less of that is likely to reach the peasant farmer or farm worker, and only slightly more reaches the manual worker in developing countries.

Not least, the multinational trend of production, trade, and payments has transformed the practice of comparative advantage on a global scale. In its later Heckscher-Ohlin-Samuelson variant, this principle is still based on relative factor proportions and comparative advantage in trade between different companies and different countries. But for decades such trade has been transcended by trade within the multinational corporation, that is, between branches in different countries. Such companies can employ lower or least-cost labor on a global scale with the highest or most appropriate technology, profoundly qualifying the capacity of developing countries to compete on an autonomous basis in the international arena. Trade liberalization and its endorsement by most international institutions, therefore, no longer automatically promotes the interests of developing countries rather than the interests of multinational companies.

In the case of the IMF, the monetarist counterrevolution legitimized the deepest instincts of the Fund on the primacy of sound money and the private market versus public spending and the social sector. The IMF indeed acts as a bank on a global scale, imposing short-term private criteria rather than looking to the long-term interests of the global economy. Although it attracts some of the brightest students of graduate schools, it is as though the IMF had stopped their thinking at term one, week one. For instance, the IMF has now imposed deflation on so many of the world economies that it has substantially contributed to global slump itself. Recently it has prided itself on turning around the import trade of some of the principal Latin American economies, converting a deficit of some $45 billion into a surplus of $30 billion. It coolly ignores the fact that it has thereby taken some $75 billion out of global demand. For one country or a few countries facing short-term balance of trade or payments deficits, such policies might be appropriate; for the global economy as a whole, they are a prescription for slump. The world does not have a global trade or payments deficit. We are not yet trading with Mars or the moon. The fact that recent OECD figures show a discrepancy of £100 billion between total country imports and exports reflects national underrecording, through inefficiency, and multinational underinvoicing in trade transactions that pass through tax havens, rather than a deficit in the real world economy.

The result is that the IMF has been imposing beggar-my-neighbor deflation on the world economy as a whole. In so doing it has sanctioned an unprecedented assault on the global mixed economy, since its recommended prescriptions on reducing money supply bite first on the public rather than the private sector. Herewith an irony and double standard: despite the fact that some of the principal subscribers of the Fund in industrial countries themselves benefit from and in large part flourish by the mixed economy, the IMF determinedly denies a mixed economy framework for developing countries.

On top of this, the Fund has imposed a succession of beggar-my-neighbor devaluations on developing countries. Again, for some countries in an expanding world economy, such a strategy could well meet with success. Recently, in some of the smaller developed countries, such as Norway, it has done so. But for developing countries as a whole, the combined package of deflation and devaluation has meant a catastrophic fall in real living standards. It is more than a straw in the wind that in some developing countries, such as Brazil, armed robberies have shifted from money and banks to food and supermarkets.

Where does the World Bank stand in all this? In one sense, very much on the sidelines. Overshadowed in its long-term development objectives by the short-term constraints imposed by the Fund, it is dwarfed by the scale of the global economic crisis and developing-country debt. In some respects the Bank is already aware of this, and signals in various degrees of code have already been received outside its Washington office. But if the Bank is concerned about global monetarism, it shows few signs of recognizing either the global colossus of multinational capital or the developing world's imperative of a mixed economy.

For some time following the OPEC price increases and the onset of beggar-my-neighbor deflation, some of the Bank's key advisers still were arguing in terms of deflation and devaluation as the keys to economic recovery. At a conference in the late 1970s on the Portuguese economy, organized by the Gulbenkian Foundation, Bela Balassa—a senior consultant to the Bank—argued that Portugal's future lay in following the example set by what are known as the "four little tigers" of Hong Kong, the Republic of Korea, Singapore, and Taiwan.

To be charitable, Balassa's recommendations were less than well informed. As the recent (1984) Institute of Development Studies (IDS) analysis has convincingly shown, Korea has a state capitalist rather than a market economy system. Its intervention includes not only rigorous import controls through licensing companies but also price controls and major state finance for capital accumulation. Korea has not been alone in following in this respect the example of Japan and its Ministry of International Trade and Industry (MITI) rather than the textbook market economics of the Fund or the Bank. Taiwan, in its own way—as illustrated in the IDS report—has done the same, quietly but extensively.

Further, being less charitable to Balassa, each of the "four little tigers" has combined major state intervention with ruthlessly repressive policies toward either the political opposition or a free trade union movement. Fascist repression rather than liberalization is typical of the newly industrializing countries of Southeast Asia. Some commentators at the Gulbenkian conference pointed out that this was precisely what a democratic revolution in Portugal had just overthrown and that they aspired to a democratic alternative.

On the question of developing markets, regrettably, the World Bank does not appear to have registered the limits to market forces in its recent pronouncements. The *World Development Report 1983* (World Bank 1983d), especially chapter 6, and the key background paper by Agarwala (1983) conclude that a third of the variation in the growth performances of over thirty developing countries can be explained by price or market distortions. The basic argument of the Bank is that, ceteris paribus, price and market distortions hinder growth through a variety of mechanisms. This covers overvaluation and exchange rate appreciation induced by the oil boom in Nigeria and Indonesia, protection, exchange rates, interest rates, social and economic infrastructure, and the general price level.

Such reasoning is fundamentally flawed on several grounds. First, it fails to take account of the role of multinational companies on the exchange rate front, their domination of the export markets of most developing countries, and their internalization through subsidiary trade of many of the gains which should accrue to national economies from increased competitiveness. Second, it fails to recognize what Evans and Alizadeh (1984) show to be the highly visible hand of the state rather than the invisible hand of the market mechanism in key developing countries, including successful newly industrializing countries. Third, it fails to admit that political repression of workers and trade unions tends to be more closely correlated with success in newly industrializing countries than does the free working of the market mechanism.

Only a handful of developing countries, just over a dozen in all, have been the beneficiaries of more than three-quarters of foreign investment by multinational corporations. Although I was sitting slightly closer to Tim Raison than in the House, I was tempted to intervene on that point. Exchange liberalization is not automatically to the advantage of developing countries in general, any more than it is to the advantage of the least developed countries. The handful of economies which are the main beneficiaries of investment by multinationals are intermediate rather than least developed, and several of them are now faced with major crises. Taiwan has found that after a period of tax holiday several multinational companies have upped and awayed to other areas in the developing world. Korea has found that its concentration on steel, shipbuilding, and automobiles may have been yesterday's investment in yesteryear's growth industries. Brazil, faced with chronic debt and a collapse of its manufactured exports to developing countries, has succumbed to the International Monetary Fund.

Some developing countries with radical governments have reacted to this crisis by pursuing a basic needs strategy. We heard that strategy endorsed by a representative of the Bank during the discussion earlier today. It focuses on housing, health, education, and social services rather than following the market formula of generating a sufficient export surplus to achieve some trickle-down effects to the poorer section of the population. Such countries—and I say this despite the case stated by the Bank—not least Nicaragua, have had short shrift from either the Fund or the Bank in terms of lending and financial assistance.

Clearly, there is as yet no broadly agreed set of social, economic, and institutional criteria on which global agreement could be achieved to promote development. Nonetheless, there is a growing argument which challenges the primacy—still reflected in much of the Bank's reasoning and many of its own pronouncements—of market forces as the determinants of relative growth performance and of market processes such as competition as determinants of economic success. In contrast to Agarwala's measurement for the World Bank of the extent of market distortions, it is clear from the newly industrializing countries that a complex social, economic, and political process has been involved in their recent, if temporary, success.

Not least, the rest of the developing world cannot develop simply by seeking to imitate the model of the newly industrializing countries. Certainly there is no way in which Sub-Saharan Africa, afflicted by debt and currently crippled by drought, can do so. The World Bank's recent initiative for Africa can be applauded on several grounds, but its stress on the free working of market forces in no way enables African countries to countervail the constraints of monetarism and multinational captial. The resources likely to be allocated to the initiative of some $500 million are derisory in relation to Africa's overall debt of some $40 billion.

Although neither the executives of the International Monetary Fund nor those of the World Bank can be held uniquely responsible for the scale of the current global crisis, there is no question that the Fund's deflationary policies in practice deepen it, while the Bank thereby is forced to apply Band-Aids through development projects to a developing world hemorrhaging with deficit and debt. If there is a leap of the imagination which must be made by the politicians of the developed countries jointly with those in the developing countries—and I stress here, in particular, the responsibilities of those developed countries that are mainly responsible for the policies of the Bank and the Fund—it will be through recognizing that only global redistribution can ensure economic recovery and that the prime needs of developing countries are in social rather than private accumulation. Housing, health, education, and social services typical of the mixed economy in industrial countries are imperative for an increase in real welfare and real living standards in the developing countries. Priority expenditure on such programs for social accumulation and distribution undoubtedly would result in sustained deficits by developing countries. But, in contrast to the limited reasoning of the International Monetary Fund, one country's deficit is another country's exports. There is no way in which the developed world can increase its exports to the developing world if, through IMF policies, the North imposes deflation on the South. This issue, in turn, relates to the global debt crisis. President Alfonsin of Argentina has excellent reason to claim that his country can repay its debts if others will buy its exports.

Global recovery itself is imperative if we are to avoid a disintegration of the world trade and payments system triggered by default on developing-country debt. The argument against recovery from market and monetarist circles focuses on inflation, but apart from the valid criticisms now made against many of Friedman's monetarists and those associated with the monetarist school, inflation in the developed world is not a problem. In some developing countries hyperinflation is chronic, but it also has been sustainable with high growth or hypergrowth—as in the case of Brazil before the recent IMF packages. One would not thank a doctor for reducing a patient's temperature if the result were rigor mortis. There is no way in which world leaders or world institutions should give priority to reducing inflation if the result is a collapse of the global economy.

How possible is recovery? A range of economists from several European countries associated with the "Out of Crisis" project have identified the scale of the world deflationary gap, the critical counterpart to the inflationary gap with which some Keynesians and all monetarists have been so concerned for the last ten years (Holland 1983; Manley and Brandt 1985). The "Out of Crisis" project has claimed that a net expenditure of $100 billion among the

European economies would sustain an increase in both U.S. and developing-country exports of some 4–5 percent a year, owing to the overwhelming share of the European economies in global trade. Such a sustained annual expenditure not only could create over 20 million jobs in the OECD countries but also could increase developing-world GNP by over half in a new development decade.

This global development push from the North clearly needs to be matched by specific development for and from the South. On the aid front, if the OECD countries as a whole were to achieve the United Nations target of 0.7 percent of GDP, and if those countries in excess of 0.7 percent were to sustain their exceptional aid programs, this not only would represent a major advance in the development prospects of developing countries but also could create an additional 2 million jobs for the OECD donors, illustrating the strength of the mutuality argument in both Brandt reports. But the crucial complementary policy, calling for endorsement by developed-country governments, lies in accepting sustained development deficits by developing countries. This means countering and reversing IMF conditionality and its twin-headed axe of devaluation and deflation.

It is time that the IMF learned to live with the mixed economy, recognize the imperatives of social spending in developing countries, and realize that an appropriate exchange rate must reflect both the social and the economic priorities of developing countries, including countervailance of multinational companies.

Faced with a second-term Reagan administration in the United States, some people might argue that such a scenario is improbable. But the case has been put. It has been endorsed, for example, by the heads of governments and leaders of parties of the Socialist International, who stressed that a net expenditure program of $100 billion is equivalent to one-tenth of the world's annual arms spending. If the developed world is seriously concerned about its own financial interests, it cannot disregard the mutual interests in joint recovery and global development stressed by the Brandt reports. If the World Bank, among others, can address itself to such problems and add its voice to the case for major redistribution and recovery programs, it could in the future perhaps step out from the shadow of the Fund as a force for global development.

Discussion

A speaker questioned whether the presentation had focused adequately on the validity of the Bank's advice to its member countries. In his view, the essential issue to be addressed was not whether the mixed economy should be abandoned—in any event, this was not being advocated by the Bank—but rather which tasks were best performed by the private sector and which by the state. It seemed to him too extreme to imply that market forces were totally unimportant, that an overvalued exchange rate was not damaging to a country's interests, or that inadequate price incentives to smallholder farmers did not hinder economic development.

Mr. Holland replied that in the presentation the case had been made for a process of social as well as private accumulation characteristic of a mixed economy, not for abolition of the market. Moreover, it had been argued that changes in exchange, tax, and interest rates did not automatically stimulate market forces in developing countries and that export-led growth was not necessarily an appropriate objective for every developing country.

A question was raised about the desirability of increased funding for the IBRD and IDA and the potentially inflationary effect in industrial countries of increased public spending on development aid. Mr. Holland noted that a larger seventh IDA replenishment would indeed have been desirable, although an increase in the IBRD's capital was less so "on its present track record." Mr. Holland spoke of the possibility of envisaging a different kind of multilateral funding for countries that were not benefiting from IBRD, IDA, or IMF support; such funding might take the form of joint programs among several donor countries directed at individual developing countries. As for public spending and inflation, there was no overwhelming evidence that a coherent international correlation existed between money supply and inflation. Moreover, there was a strong case for saying that deflation could be inflationary: that as the rate of growth of a market declined, the big businesses in price-making positions on a global scale (such as were found in commodities and food markets) could and did compensate for falling sales by raising prices.

Another speaker raised several specific points about the World Bank's role, and replies followed. The first question concerned the Bank's willingness to accept the premise that export-led growth, particularly in manufacturing, would not be feasible for a second or third generation in all developing countries. It was stated in reply that the assumptions underlying the Bank's policy advice were that resources had to be used efficiently and that the scarcity of oil resources had to be reflected in the pricing of the factors of production. If prices were substantially distorted, the result could be an investment and production structure of the economy that did not utilize domestic resources reasonably. Obviously, it would not be appropriate for every developing country to model itself on Korea or Taiwan.

With regard to the sustainability of balance of payments deficits by the poorest countries and the financing of the imbalances, the point was made that these were the foundation stones on which Bank and IDA lending were built. For the poorest countries, the capital for financing their development needs had to be supplied on grant or low-interest terms; for middle-income countries with high-interest debt burdens, the development planning equation had to take account of the debt-servicing problem.

As for the desirability of decreased state intervention in economic activity and of exchange rate neutrality with respect to imports and exports, it was noted that the Bank operated within the economic framework chosen by its borrowers which, in many cases, included large public sectors. The Bank saw its role as drawing to the attention of governments the consequences of actions or inaction for the efficiency of resource utilization and for domestic resource mobilization in each country.

In the view of another speaker, the presentation did not distinguish adequately between the Bretton Woods institutions and the governments which supplied them. With regard to the Fund, there were two separate issues. One concerned the Fund's resources and its capacity to permit countries a slower and more reasonable period of adjustment. The other related to what the Fund did with given resources and what programs it devised for its client countries. It was in this area especially that the speaker felt the presentation had overlooked the existence of successful Fund programs and of instances in which relations between the Fund and the country were good, even in Africa. As for the Bank, it did not have a "mad private-enterprise orientation." Rather, it followed a sophisticated approach in considering prices and their effects on efficiency. This speaker would have found it beneficial for the presentation to have distinguished between sensible uses of price mechanisms and the use of market forces more generally.

According to the same speaker, the real mystery concerned relations between the Fund and the Bank, which were in a fairly poor state despite efforts to improve them. The Bank was only peripherally involved in negotiations with the big Latin American debtors, although it participated more directly with the Fund in framing public investment programs in the poorest countries.

Mr. Holland observed that the countries whose multinational companies dominated developing-world trade were the very ones that were setting the harsh tone of Fund and Bank adjustment policies in developing countries. Those countries were advocating a greater role for the free play of market forces without due regard to social factors or to the benefits of mixed economies.

The Role of the World Bank in a Maturing Capital Market

Michael Beenstock
Professor, City University Business School, London

SYNOPSIS. The fungibility of aid money makes it impossible to assess whether assistance from the World Bank has helped or hindered economic development. This line of reasoning (first developed when Professor Beenstock was on the staff of the Bank) holds that the borrowing governments request and obtain financing for "good" projects that will yield rates of return deemed suitably high by the Bank, but that they actually use the money to finance low-yielding or marginal projects. A "project possibility curve" illustrates the point.

Although the data gathered by the Bank's Operations Evaluation Department attests to a remarkably successful implementation record for Bank-financed projects, no method has been devised to track and evaluate the marginal projects being carried out under the cover of Bank financing for high-yielding projects.

The fungibility problem is a relatively recent phenomenon. From the time of the Bank's founding until the 1960s there were no competing sources of finance for reconstruction and development projects, and the IBRD was in a position to control how its funds were used. During that period the Bank certainly did assist economic development, but for some time the Bank has been competing with others in the international capital markets to lend money for projects and has been facing the fungibility trap. One way in which the Bank seems to be dealing with the problem is by moving away from project-related lending to program lending, in which money is made available in return for a commitment by the borrowing government to bring about policy changes stipulated in the loan agreement. The IBRD has perhaps outlived its usefulness as a project-financing entity and is now functioning mainly as a high-class consulting organization that provides valuable technical assistance. Indeed, the future rests not with the IBRD—which lends to sovereign governments that are

notorious for shooting themselves in the feet by embarking on economically unnecessary projects—but with the International Finance Corporation (IFC), which lends to the private sector, where the profit motive imposes a certain automatic discipline and the fungibility problem is negligible.

> *As a rule the Bank's loans will not take the form of free cash in the hands of the borrower, which he could use and squander as a free addition to his income, as was so often the case in the past. They will be tied to overseas expenditure—on specific projects, which have been carefully examined and approved.*
>
> J. M. Keynes, July 1944

On the face of it, the evidence seems incontestable: the World Bank has, on the whole, been a net contributor to the economic development of the developing world. Table 1 summarizes the distribution of economic rates of return for 183 IDA projects up to 1981. The average rate of return was 17.9 percent a year, although 19.6 percent of the projects had rates of return of less than 10 percent. Since the Bank's minimum planning return is normally 10 percent, this means that roughly 20 percent of IDA projects underperformed by the Bank's exacting standards.

The data in table 1 were calculated by the Bank's Operations Evaluation Department (OED). This audit function is not as incestuous as it seems, because the OED reports directly to the Bank's Board of Executive Directors. It should also be pointed out that the data are not true rates of return because

Table 1. *Rates of Return for IDA Projects, by Region*

	Number of projects				
Rate of return	*East Africa*	*West Africa*	*South Asia*	*Total*[a]	*Percentage of all projects*
Negative	5	7	0	16	8.7
0–9 percent	6	8	3	20	10.9
10–19 percent	24	16	20	82	44.8
20–29 percent	6	10	7	37	20.2
30–39 percent	2	2	6	6	8.8
40 percent and over	0	2	4	12	6.6
Total	43	45	40	183	100.0
Average rate of return (percent)	13.2	14.7	22.5	17.9	

a. Includes projects in North Africa, Middle East, East Asia, and Latin America.
Source: World Bank (1982), p. 63.

in many cases the projects have not run their full course, even if the Bank's involvement has. Rather, they are reestimated rates of return and are OED's best guess of the true prospective rates of return.

The OED data in table 2 show that up to 1981 the rates of return on 273 IBRD projects were broadly in line with those of their IDA counterparts. This is to be expected because the Bank claims that it selects IDA projects with the same rigor as it does its IBRD projects. More recent data, from the World Bank's *Ninth Annual Review of Project Performance Audit Results* (1983c) show that rates of return on Bank projects have been holding up well. The average rate of return is 22 percent.

Rate of return	*Number of projects*	*Percentage of projects*
Negative	0	0
0–9 percent	17	24
Over 10 percent	53	76

Figure 1 plots the average rate of return on all projects (weighted by investment cost) on the basis of recent OED annual reviews. The data reviewed suggest the following conclusions:

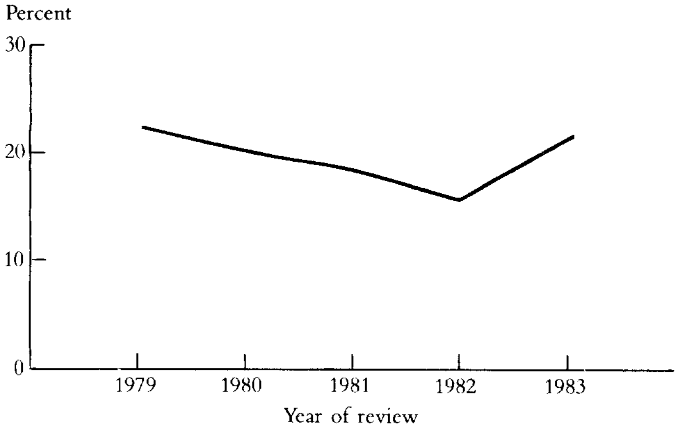
- Project rates of return average about 20 percent.
- These rates of return are achieved for the main sectors (table 2) and for most regions, with the possible exception of Africa (table 1).

Table 2. *Rates of Return for IBRD Loans and IDA Credits, by Sector*

	IBRD loans		*IDA credits*	
Sector	*Number of projects*	*Average rate of return (percent)*	*Number of projects*	*Average rate of return (percent)*
Agriculture	74	14.2	95	19.5
Infrastructure	89	14.1	24	15.2
Energy	54	14.2	11	10.3
Water supply	17	8.0	5	16.6
Telecommunications	18	19.6	8	21.1
Transport	97	22.0	59	16.4
Industry	13	15.4	5	15.0
Total	273	17.0	183	17.9

Note: Data do not include twenty-eight projects that had a blend of IBRD and IDA financing.
Source: World Bank (1982), p. 63.

Figure 1. *Average Rates of Return on World Bank Projects*



Source: World Bank (1983c), p. 17.

- About 20 percent of projects yield less than the Bank's target rate of return of 10 percent. When projects are weighted by investment cost, however, the failure rate is lower, suggesting that small projects have higher failure rates.
- There is no significant difference in rates of return for IDA and IBRD projects.

With interest rates considerably below 20 percent, it must have been the case that the net present value of the Bank's projects was substantially positive and that the projects have, on the whole, added to the wealth of the Bank's clients.

Caveats. Even if we accept the OED data at face value, it does not necessarily follow that the evidence cited implies that the Bank has contributed to development. The first caveat relates to the concept of fungibility; the project the Bank is financing is not necessarily a project the client would not otherwise undertake. This problem has been noted by the Bank itself (World Bank 1982, p. 63):

> The generally high rates of return on IDA projects can give a misleading impression, however, of the projects' impact on development. If IDA chooses the best projects, it may be leaving the others for funding by governments or other donors. Its true impact is the rate of return on the marginal project that would go unfunded if IDA resources were unavailable. It is impossible to tell, however, whether these projects differ from those actually funded by IDA and whether their rates of return are significantly different.

The second caveat relates to the appropriate cost of capital, when adjusted for risk. To determine whether a project has positive net worth, it is necessary to discount the cash flows at the risk-adjusted cost of capital. If the risks are high a 17 percent prospective return might imply a negative net worth. Correspondingly, if the risks are low a less impressive return might be compatible with positive net worth. Therefore, rates of return per se could give a misleading picture of the Bank's contribution to economic development.

The issue of appropriate risk adjustment begs fundamental questions about the Bank's function in the international capital market. It is impossible to gauge the Bank's contribution to development independently of its role in this market. Therefore, looking at rates of return and other indicators is not enough to judge whether the Bank is appropriately filling a vacuum in the international capital market and thereby promoting development that would not otherwise occur.

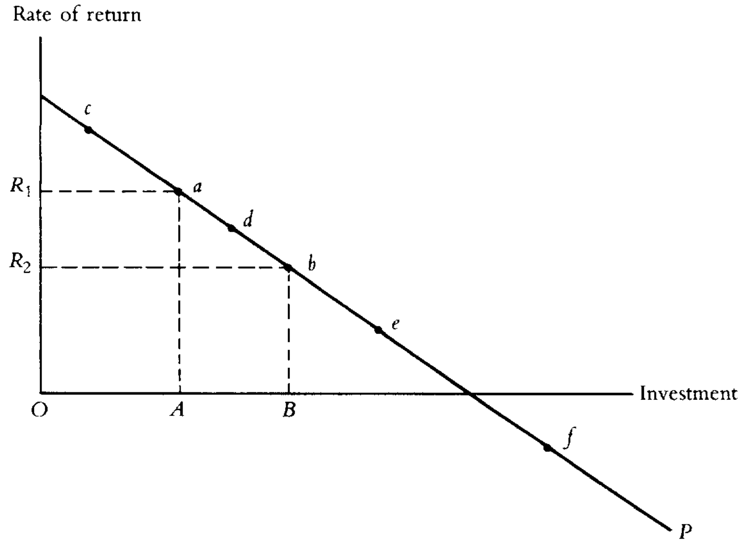
In the next section, the implications of fungibility for evaluating the Bank's role in the development process are explored. It is argued that the evidence presented above cannot be used to determine whether the Bank has aided or impeded economic development. More importantly, fungibility implies that the project cycle is little more than a charade played out of ignorance or a concern for cosmetic exercises in public relations. This in turn begs questions about the Articles of Agreement, in which the Bank is required to engage primarily in project lending.

In the section on the international capital market, the second caveat is developed further. It is argued that 1985 is not 1945 and that the international capital market is quite different from that envisaged by the Bank's founding fathers. In particular, the international capital market has matured, and IBRD clients as well as some IDA clients have access to what has emerged as a competitive international capital market in which capital costs are adjusted for sovereign risk. The efficiency vacuum that the Bank has been filling in the international capital market has been withering away, and the Bank's net contribution to economic development has been vanishing.

Finally, I discuss the future of the Bank in the light of these arguments. It is stressed that the reference to rates of return and net worth as measures of economic development are illustrative and that the Bank's contribution to development must take broader developmental issues into consideration. In other words, rates of return, important as they are, only illustrate the basic logical difficulties that circumscribe the Bank's role.

Fungibility. In figure 2 line *P* plots the hypothetical relation between investment in various projects and the projects' rates of return that faces a

Figure 2. *The Fungibility Problem*



developing-country government at a given time. The *P* schedule ranks projects according to their rates of return; a rational government would finance the projects with the highest returns first. If the government had *OA* of its own resources for investment, it would be in the best interests of the country to use them to invest up to project *a*, in which case the rate of return on the marginal project would be R_1.

If the Bank lends *AB* to the government at a rate of interest below R_2, projects along the *ab* segment of the *P* schedule can be financed. The rate of return on the marginal project is R_2, but since this exceeds the rate of interest, the net worth of the country has increased and development has taken place.

It does not really matter whether the Bank's lending is being used to finance project *c* or project *d*. If it is processing project *c*, the OED will discover that the Bank's project has been very successful; if it is processing project *d*, the OED will conclude that the Bank has been less successful. Whether project *c* or *d* is being financed by the Bank is irrelevant because the marginal project brought about by the Bank's involvement is project *b*. If it made the Bank feel more comfortable, the government could let the Bank finance the strong projects above *a* so that the OED could write a glowing report, while the government used its own resources to finance the projects below *a*.

Of course, the OED should be evaluating project *b*, but it is in no position to do so. A properly run national ministry of planning will form estimates of R_2, but it is unlikely to divulge this information to the Bank or to any external agency. Despite all the effort that goes into the project cycle, the Bank cannot know what project it is really financing. Its only consolation is that project *c* was well supervised and well implemented.

Under the assumptions stated, project *b* generates positive net worth because the rate of interest is below R_2. But if the rate of interest is greater than R_2, the net worth of the marginal project will be negative and development will be reversed rather than enhanced. In this case the Bank could be funding project *c*, which has positive net worth, when in reality it is enabling the government to finance project *b*, which has negative net worth. Indeed, matters could be worse than this because the marginal project might be *e* or even *f*.

So, the OED data presented above do not enable us to determine whether the Bank has been promoting development. Without information about the marginal project, we can never know. Indeed, the Bank itself admits as much, as the passage quoted above confirms. It is disturbing that an organization such as the Bank cannot demonstrate that it has in fact been promoting development.

It should be stressed that figure 2 does not in any way prejudge the nature of the development process. If there is a synergy between different projects, the *P* schedule will either be flatter at a given time or will shift to the right over time at a relatively more rapid rate. It simply must be true that at a given time some projects are more attractive than others. This is all that figure 2 implies.

The fungibility problem does not arise to the same extent with private sector borrowing because the private sector is unlikely to undertake projects that will impoverish it. Unfortunately, the same cannot be said about the public sector, which can sustain losses on projects that it can finance out of taxation. There is no inherent discipline that will prevent the net worth of the marginal project in the public sector from being negative. Indeed, the marginal project could well be the purchase of armaments or some other extravagance that is quite unrelated to the economic development of the country; we shall never know.

Where does fungibility leave the Bank? The Articles of Agreement require the Bank to finance projects. Unless the Articles are altered, fungibility places an enormous, if not impossible, burden on the country economists to estimate the rate of return on the marginal project. Alternatively, the attentions of the OED should be switched to this more pressing problem. Various methodologies suggest themselves, but I shall not consider them here. In any case, they would be speculative and may not generate reliable estimates about the marginal project. In the meanwhile, the Bank should ask itself the following questions.

- Is project *c* likely to be financed in any case? (If the answer is yes, the Bank should not finance it, no matter how impressive it might look in an OED report.)
- Is the government likely to finance projects *e* or *f*? Will it undertake these projects regardless of what the Bank does? (If both answers are yes, the Bank should fund project *c*, for otherwise it will not be implemented. If the answer to the second question is no, refusal to fund *c* might prevent the government from going ahead with *e* or *f*.)
- Does the Bank provide the bulk of investible resources? (If it provided 100 percent of these resources, its marginal project and the government's marginal project would be identical. The Bank would then have no need to fear fungibility.)

In answer to the last question, table 3 offers little comfort. The first two panels report the share of IDA in the investment of specific developing countries. The third panel reports the proportion for IBRD loans. On the whole the Bank's assistance is marginal, at least as far as total investment is concerned. Most probably, these data exaggerate the Bank's lack of leverage, which would be better expressed in terms of public sector investment than in terms of total investment; such data, however, are not readily available. Nevertheless, table 3 suggests that, as a peripheral source of finance, the Bank is likely to be greatly exposed to the fungibility syndrome.

The International Capital Market. In 1943 Harry White and John Maynard Keynes envisaged a postwar world bereft of a properly functioning international capital market. Apart from the effects of the war, the international capital market had been disrupted by the economic and financial turbulence of the interwar years. Economic reconstruction would have to be financed in the war-torn countries, while economic development in the poorer countries of the world would also need finance. But without an international capital market, reconstruction and development would be jeopardized. White and Keynes intended the Bank to fill this vacuum.

The Bank was therefore designed to counterbalance a market imperfection; it would finance sound projects which for various reasons would not otherwise be financed by the international capital market. Since 1945 the international capital market has staged a more or less complete recovery. The Eurocurrency markets came of age in the 1960s, and the Eurobond markets emerged in the 1970s. Where once the Bank stood alone in the medium-to-long-term capital market, it is now in good company. Indeed, in many cases

Table 3. *World Bank Leverage*

Country	*IDA as share of investment, 1980 (percent)*	*Country*	*IBRD lending, FY 1984 as share of investment, 1982 (percent)*
Chad	1.1	Indonesia	5.1
Bangladesh	13.1	Korea	4.0
Ethiopia	7.9	Nigeria	2.2
Nepal	9.4	Malaysia	0.7
Somalia	3.9	Philippines	1.5
Guinea-Bissau	2.3	Brazil	2.7
Burma	2.2	Colombia	4.5
Afghanistan	3.5	Mexico	1.6
Mali	9.2	Peru	3.2
Burundi	10.0	Turkey	17.8
Rwanda	5.7	Morocco	6.6
Burkina Faso	4.9	Egypt	5.0
Zaire	3.8	Yugoslavia	2.1
Gambia	7.7		
Haiti	5.0		
Sierra Leone	1.4		
Tanzania	3.1		
Guinea	5.1		
Central African Republic	15.3		
Uganda	0.5		
Benin	5.6		
Niger	2.7		
Madagascar	2.5		
Sudan	3.6		
Ghana	1.1		
Lesotho	3.1		
Yemen, PDR	3.7		
Yemen Arab Republic	1.8		
Mauritania	1.5		

Sources: IDA, World Bank (1982), p. 92; IBRD lending, World Bank (1984a), pp. 139–40; 1982 investment, World Bank (1984b), table 5.

the Bank is in direct competition with the private international capital market. It has become increasingly difficult to see the imperfection in the capital market that the Bank has been rectifying, especially in relation to its IBRD business. Correspondingly, it is increasingly difficult to appreciate the Bank's role in the development process. Moreover, the Bank has two fundamental advantages over its private competitors. Because the Bank's capital is subscribed by member governments, World Bank bonds are more or less gilt-edged. If its loan portfolio ever got into difficulty, the Bank would draw on its unpaid-in capital to meet its liabilities. Since the Bank is completely unlevered, it can never default—provided, of course, that the unpaid-in capital is indeed callable. Slight changes in the Bank's bond ratings can be understood only in terms of doubts about callability.

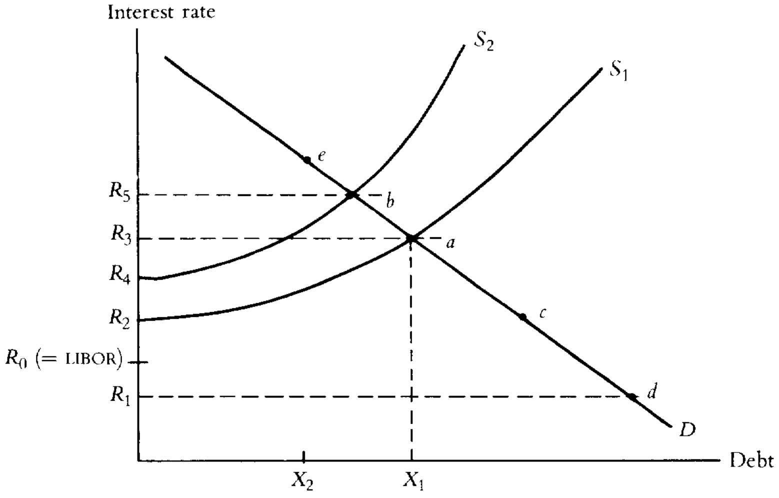
Since the Bank can borrow at better rates than can its competitors, it is at an advantage in competing for loans. At the same time it has another advantage in that sovereign clients prefer to default with other banks rather than with the World Bank. Indeed, the Bank takes considerable pride in the fact that it has never experienced a default and that rescheduling is a rarity. It certainly has never required the services of the Paris Club, at a time when other banks have been less fortunate. This default preference reflects the Bank's political importance. Brazil is naturally less inclined to default with the Bank, of which it is a member, than with Chase Manhattan, of which it is not.

Given its capital structure and the recovery of the international capital market, how should the Bank operate in the presence of sovereign risk? Keynes (1980, pp. 74–75) took the view that sovereign and country risk was something that the Bank should ignore:

> In the dangerous and precarious days which lie ahead, the risks of the lender will be inevitably large and most difficult to calculate. The risk premium on strict commercial principles may be beyond the capacity of an impoverished borrower to meet, and may itself contribute to the risks of ultimate default. Experience between the wars was not encouraging. Without some supporting guarantees, therefore, loans which are greatly in the interests of the whole world, and indeed essential for recovery, it may prove impossible to float.

To explore some of these issues, we use figure 3. The vertical axis measures interest rates and the horizontal axis measures the sovereign debt of a developing country. The *D* schedule represents the demand for sovereign debt by the developing country and is based on the *P* schedule in figure 2. The higher the rate of interest, the lower is the desired amount of debt by a developing country because the number of profitable projects is smaller. The S_1 schedule represents the supply schedule of sovereign loans. It is upward sloping because risk exposure increases with the amount lent and the elasticity of S_1 varies inversely with risk tolerance in the international capital market and the nondiversifiable element of country (sovereign) risk. Schedule S_2 represents the lending schedule for a second developing country for which sovereign risk happens to be greater. In the former case the basic

Figure 3. *The Market for Sovereign Loans*



Sources: Beenstock (1984); Heffernan (1985).

sovereign risk premium expressed as the margin above the London interbank offered rate (LIBOR) is $R_2 - R_0$; in the latter case it is $R_4 - R_0$. As a gilt-edged borrower, the IBRD has a rate that is represented by R_1, so that $R_1 - R_0$ is the risk discount that reflects the Bank's capital structure and guarantees.

In the case of the first developing country, the sovereign loan market is in equilibrium at *a*, where S_1 intersects *D*, and the competitively determined interest rate is R_3. This is the rate of discount that the government and the Bank should apply to the projects being appraised. The project represented by *c* would have a positive net present value at the IBRD rate (since at this rate *d* is the marginal project) but not at the market rate, R_3. For the second developing country, the market rate would be R_5.

The analysis of figure 3 serves to remind us that the Bank's contribution to development cannot be gauged independently of its role in the international capital market. The analysis implies that the appropriate discount rate is not the IBRD rate or LIBOR but the market-determined rate on sovereign loans. Moreover, these rates vary from country to country. For example, a sample of loan agreements signed in London in 1983 suggests that the range can be as wide as 3 percentage points.*

The Bank is enjoined to lend at the IBRD rate, and it cannot charge different rates to different countries. This implies a subsidy of $R_3 - R_1$ to the first

*I am grateful to Shelagh Heffernan for these data.

developing country and a larger subsidy of $R_5 - R_1$ to the second developing country. Insofar as this subsidy enables the first country to finance project *c*, the Bank's contribution to development will have been negative despite the OED claim that at the Bank's lending rate the project's net present value is positive. The same applies to project *a* in the case of the second country.

So far we have been assuming that the international capital market is competitive and efficient. In such a world the Bank cannot make a positive contribution to development; at best its contribution is neutral. The same does not apply if the international capital market is inefficient. For example, say that the first developing country wants to borrow X_1 when the sovereign lending rate is R_3, but the capital market sets a credit limit at X_2. In this case the marginal project will be *e*. The international capital market might behave in this way if sovereign borrowers were threatening to default, as discussed, for example, by Eaton and Gersovitz (1981), or as in 1945, when the capital market was disrupted. In the face of such imperfections, the Bank will contribute to the development of the first country if it finances projects along the *ea* segment of schedule *D*. For the second country the corresponding segment will be *eb*.

In 1945, X_2 showed little prospect of approaching X_1, and there was a clear need for the Bank to compensate for imperfections in the international capital market. By 1985 the gap between X_2 and X_1 had shrunk to zero and so had the Bank's constructive ability to fill a void in the market. In the meanwhile, governments seek Bank loans because they can borrow at a subsidized rate. And to salve the Bank's development conscience, the government offers the best projects for evaluation while it uses the subsidy to finance submarginal projects through the logic of fungibility.

The Future of the Bank. Before the recovery of the international capital market (when X_2 was considerably smaller than X_1), the Bank naturally had more leverage over its clients. In a world starved of capital, lenders carry abnormal amounts of clout. As the Bank increasingly finds itself in competition with the private capital market, it has felt its authority undercut. Simultaneously, and for related reasons, thinking people at the Bank have been aware of the fungibility problem and realize that OED results do not properly measure the success of the Bank. Fungibility implies that project lending is indeed program lending by another name. Although nobody has been so bold as to declare the emperor naked, structural adjustment loans (SAL) are to be understood in this light.

SALs throw over one pretense but replace it with another. The pretense underlying SALs is that policy reforms require finance and that fungibility does not apply in this case. Projects obviously need finance, and balance of payments adjustment needs finance, but it has never been established why reforms in agricultural pricing and the implementation of other forms of sound developmental advice should automatically need finance.

The basic question is whether a SAL can induce desirable policy changes which would otherwise not have taken place, irrespective of whether the policies require finance. If the answer is yes, the SAL can be regarded as a benign bribe. In an imperfect capital market the Bank may be able to undertake such a role, but it is difficult to see how it can do this when other lenders are in the market at the same time. If the policy changes are implemented, it is unlikely that this was because of the SAL, since the government would have been able to borrow elsewhere in any case.

The rise of the SAL is therefore a symptom of the Bank's increasing difficulty in discovering a meaningful niche for itself in the development process, rather than a resolution of this basic problem. In contemplating its future, the Bank should not take its own role for granted. Forty years after Bretton Woods, the burden of proof rests with the Bank and its supporters to justify its continued existence rather than the other way around, as was the case in 1945. Accordingly, the Bank should inaugurate research into the following areas.

- Theoretical and empirical research into the fungibility syndrome in relation to IDA and IBRD lending
- The development of methodologies to identify the shadow or marginal project
- The identification of breakdowns in the international capital market which distort the allocation of capital to individual developing countries
- A critical review of the Articles of Agreement, especially in relation to the interface between program and project lending
- A review of the relation between the IBRD and the IFC, since fungibility is not so relevant to IFC lending.

Discussion

The presentation generated a flurry of comments, some delivered in slightly indignant tones. One speaker felt a paper should have been written entitled "Fungibility and Common Sense." He pointed out that 54 percent of the gross investment of the low-income countries of Sub-Saharan Africa had been financed with net aid, most of it effectively coordinated by the Bank through donor consortia. When such a large proportion of investment was financed by aid, it could not be argued credibly that all that extra money would have been spent anyway on the same development projects. These projects could never have been carried out without the expertise in project analysis and preparation and the technical assistance that came along with the Bank's cash. Thus, it could not be argued that there was total fungibility on the recipients' end; on the contrary, the donors held a lot of leverage over the recipients, but there was no corresponding leverage on the donors. The speaker suggested that fungibility should be looked at in the context of donors' actions. If the money appropriated by donor governments for IDA replenishments had not been channeled into the World Bank/IDA, it would most likely have gone instead to finance the marginal and worst projects of the donor government, since IDA had absolutely no leverage on the lending governments, in contrast to its considerable leverage on borrowing ones.

Beenstock conceded that channeling over half of a borrowing country's net aid through donor consortia did indeed provide the latter, including the Bank, with significant clout with respect to the borrower, although it was still not necessarily enough to overcome the fungibility problem entirely. In any event, the thesis had focused on IBRD lending rather than on IDA assistance.

Another speaker criticized as uncreative and unconstructive the paper's unwillingness to see the resources of the World Bank used to strengthen the role of governments in helping their nations to progress and develop successfully. He suggested that it was legitimate to use World Bank development funds to ensure that policy analysis and policy management were handled satisfactorily by the borrowing-country governments.

What would happen to the theory of fungibility, asked a different speaker, if the curve looked completely opposite, that is, if it looked like a learning curve in which the worst possible, lowest-yielding projects were the first ones to be financed by Western donors and aid agencies? Perhaps this was what had occurred in the 1950s and 1960s, when overly ambitious industrialization projects were undertaken but agriculture was seriously neglected, and that had given development assistance a bad reputation.

Another speaker remarked that the grain of truth that could be found in the fungibility argument had been put into a hothouse where it had turned into a rather exotic bloom. He pointed out several fallacies in the argument. The first error was in hypothesizing that there was a single set or line of projects running down to the low-yielding ones. This did not take account of the dynamic movement over time of the project possibility curve as projects, their rates of return, and their relations to each other changed. A second fallacy in the argument was that it overlooked the transformation that occurred in the projects themselves through the aid process. Far more than money was being transferred; various components designed to increase the projects' effectiveness, such as institution-building and technical cooperation, were included in the package. Thus, it was a gross oversimplification to depict the Bank as no more than a superior consultancy firm. Its operations involved dialogue between the donor and the recipient not only on the project itself but also on other policy-related issues. The importance of the World Bank as an institution, this speaker stated, rested not only on its project work and associated dialogue but also on the conscious effort it was now making in the areas of policy reform and aid coordination. Structural adjustment lending was not merely another version of fungibility. Rather, it was crucial to what was going on in the aid world today. Although project lending might still dominate in terms of volume of resources transferred, the concentration of efforts was on devising and putting in place a wide range of policy reforms, such as those on agricultural prices and exchange rates that some fifteen to twenty African countries had recently undertaken in relation to Bank and other programs.

The same speaker conceded that there was some validity to the fungibility argument in connection with IBRD lending to relatively well-off developing countries which had the option of borrowing easily in other markets and for which Bank financing represented a small proportion of their total external finance. This situation, however, was confined to a relatively small number of countries. Many others were "blend" countries that borrowed a mix of IBRD and IDA money. He concluded by noting that "when aid goes awry, it is scorned and held up as proof that aid does not work. But when a private sector investor fails and goes bankrupt, nobody thinks it calls into question the private enterprise system."

Responding to the chorus of critical comments, Beenstock conceded that he had put the argument forward in simple terms, but he did not agree that his analysis was simplistic. He reiterated that the fungibility problem was a fundamental one and that the Bank itself was well aware of the problem, as illustrated by the passage from *IDA in Retrospect* quoted in his paper.

The World Bank and Economic Policy in Developing Countries

S. Shahid Husain
Vice President, Operations Policy, The World Bank

SYNOPSIS. In the past the relation between the Bank and its borrowers centered on specific productive projects; that relation has evolved to include an in-depth dialogue on an array of macroeconomic issues that shape the policy environment in which projects are undertaken. Among the new instruments devised to carry out that dialogue are structural adjustment loans (SALs) and sector loans. SALs are basically program loans with performance links to specific actions to be taken by the governments in four areas—efficiency of resource use, mobilization of domestic and external resources, trade, and institutional development. Sector loans are similar to SALs: they essentially make Bank assistance contingent on the government's taking certain measures to deal with various problems in the sector. The quest for policy improvement has not supplanted the Bank's concern for poverty alleviation. Rather, the Bank believes that more progress towards poverty alleviation can be made in the context of an overall policy and institutional environment that supports national economic growth and efficient use of resources. Two examples (Indonesia and Turkey) illustrate that the Bank does not approach policy dialogue rigidly. Indeed, the Bank is keenly aware of the need to demonstrate humility and sensitivity to each country's unique circumstances and concerns.

I shall try to be brief, and what I will do is to trace the evolution of the Bank's operations and the shifts in emphasis. I will try to describe how we approach our lending today, how we make our decisions on the basis of economic circumstances and the country's circumstances, and the issues that we see in our relations with developing countries.

If we look at an IBRD or IDA operation, its basic composition is a mixture of support for specific investments or programs of investments, measures for institutional development, manpower training and organization, and policy change. The mix varies with countries, and it has varied with time.

If we go back to the beginnings of the Bank and trace the evolution of our lending, apart from the initial period of reconstruction and support of European countries, the early period was marked by a substantial emphasis on capital accumulation, and the Bank's operations were largely concerned with infrastructure. Electric power (there was a lot of electric power financing, particularly in Latin America) and transport were the two main areas.

As we came into the 1960s and early 1970s, we understood, and everybody else understood, that there had to be a broadening of concern; hence the emphasis on agriculture, on education, and later on urban development and population planning. Of course, in the middle of the period there was tremendous concern with the distribution of the benefits of economic growth. We realize that economic growth does not necessarily ensure a reduction in poverty. But a fundamental thought in this effort for poverty alleviation was that, while basic needs had to be addressed, ultimately there would be little progress in the alleviation of poverty unless progress was made in improving the productivity of the poverty groups—the small farmers, the landless, and the urban poor. That had to be an important element in our focus on the alleviation of poverty.

With the two big increases in oil prices in the 1970s, particularly in the late 1970s, and the subsequent economic efforts of the early 1980s, the situation became particularly complex and difficult in many developing countries, largely because of the severe limitation on the availability of resources, domestic and external, in most of them. You may remember that after the second oil price increase there was a substantial expansion in the balance of payments deficit of the oil-importing developing countries in the late 1970s and the early 1980s, with balance of payments gaps of the order of 6, 7, 8, or 9 percent of GNP becoming fairly common. Many people thought that this was not tenable in terms of availability of capital or in terms of the management of resources. It therefore became increasingly apparent that not only was investment important but so was the overall policy environment in which investments were made.

Also, we had evidence from our own experience over the years—largely through our own operations evaluation and through our continued relations with developing countries—which showed that many a good, well-conceived, well-formulated project foundered on poor policy. There could be a perfectly good agricultural project, the project could be implemented, the irrigation channels could be there, and so on, but the farmers would not respond, simply because the overall pricing policy militated against the effort. The same might be true in industrial areas or in many other fields. Hence the growing concern with the policy environment, the institutional environment, and the relation between the Bank and the developing countries.

It would be wrong to say that we only discovered the importance of policy in the late 1970s or the early 1980s—the importance of the policy environment had been known for a long time—but the emphasis had changed. If we look back at some of the earlier loans that the Bank made for electric power, we were concerned with the overall efficiency of power investments and with the resource position of power entities, and you would routinely find in the loan covenants concern about financial rates of return and power tariffs. Going back to the 1960s and taking a country like Brazil, for example, where the Bank's lending for electric power was fairly extensive over a period of time, we had a substantial dialogue with the Brazilians, not simply on specific power entities but on the overall investment program over a period of time in the power sector. We have carried on extensive economic work and sector work in all the countries to which we have lent, and these have provided the occasion for a dialogue between the Bank and those countries. Until about five or six years ago, however, there was essentially a limited relation between the Bank and the developing countries. It was a lending relation, and the conditionalities and the performance criteria were essentially related to the specific subject of the loan. In parallel to that there was the economic work, the economic assessment, and the economic dialogue, but the link between operations and economic performance or economic conditionality was at best tenuous. There were times when we suspended lending to countries—we did not lend to Brazil, for example, for seven or eight years in the late 1950s and early 1960s, and there were similar periods when we did not lend to other countries. These were occasions when the so-called deterioration in economic performance was extreme and we had severe doubts about the creditworthiness of those countries.

What essentially has happened in the past five or six years is a growing dialogue and relation between countries and the Bank over a spectrum of economic issues—dialogue on macroeconomic issues, which means the overall pattern of resource use, the overall efficiency of resource use, a variety of issues of resource mobilization, the relation between government and the public sector (a relation which basically governs the use of resources in the public sector), and the mobilization of these resources in public enterprises in a large number of developing countries. The area of concern of the government is, after all, very wide. Public enterprises have a tremendous impact on the overall pattern of resource use and resource mobilization and on production and growth. Hence a substantial part of our dialogue concerns the operation of public enterprises.

Investment programs and resource use have come into focus in the context of trade and exports. Our initial concern about these issues arose at the beginning of the second oil crisis, when a number of us felt that the balance of payments deficits were not tenable. One of the points we are making is that if, within the limits of the prospective availability of capital, the process of economic development is to be viable, economies have to have substantial flexibility in responding to changes in circumstances and changes in the economic environment. One of the particular issues here is the external trade regime in which countries work: what are the policies with regard to exports, and how do tariffs, exchange rates, and investment policies discriminate against exports? Beyond that, what sort of signals do government policies convey to the economy at large in response to changes in demand and supply patterns?

Concurrently with these concerns and dialogues, obviously the instruments and the media through which we conduct our dialogues have changed. We still finance investments—the bulk of the Bank's lending is related to specific investments—but we have devised other instruments which are the basis of this dialogue. We have the so-called structural adjustment loans, which are basically program loans with a fair number of performance links with specific programs to be adopted by governments in, basically, three or four areas. The first area is efficiency of resource use, and that covers investment programs, the relation between government and public enterprises, and the relation between government and the private sector. The second area is domestic resource mobilization and the use of external resources. That covers such areas as the generation of resources by public enterprises, the generation of resources by government, interest rate policies, regulation, and so on. The third area, which is an area of particular focus for us, is the foreign trade regime. That covers the sort of incentive that exists for exports and the biases in the system of trade and tariffs which affect the relative priorities of import substitution and exports. The fourth area is institutional development. Our concern is not simply that certain agreed actions be taken at particular moments; a bigger concern is that changes and policy improvements should have an institutional anchor. That means essentially that it is not sufficient that a resource generation of *X* percent should be achieved and that public investment should be *Y*; attention has to be paid to the processes and the procedures through which they become part of the institutional equipment.

We also do similar lending in particular sectors such as the agricultural sector, the power sector, and so on in which our assistance is tied to specific actions within those sectors to improve the effectiveness of resource use, the effectiveness of investment, resource mobilization, and institutional improvements within specific sectors. A case in point is Sudan, particularly the Jezira scheme. We have made loans for the rehabilitation of Sudan's agricultural sector, which had deteriorated because the price environment had led to a decline in cotton production. The purpose was not only an improvement in the policy framework but also the adoption by the government of a program for the rehabilitation of the infrastructure.

There are two or three questions that are relevant here. The first is, what are the limitations of this approach? Before I deal with that I want to say that it would be wrong to assume that in the quest for policy and institutional improvements we have somehow jettisoned our prior concerns about investments, poverty alleviation, and institutional development. The bulk of the Bank's assistance to developing countries is still investment-related, and the bulk of those operations which are investment-related are still related to specific investments. Hence, in areas such as agriculture we continue to focus on small farmers and on small-scale agriculture. Agriculture remains the single largest activity of the Bank; close to 30 percent of our lending is for agriculture. That is supplemented by our concern for institutional development. Education remains an important area of the Bank's assistance, and a significant part of our lending goes for things like slum improvement and low-cost housing in urban development programs.

We also think that poverty alleviation is a broad issue and requires simultaneously a growing national economy and an effort to mobilize national resources. Unfortunately, in a large number of countries which are among the lowest-income countries in Africa, the whole process of economic growth has come to a halt and we have had stagnation and decline on a massive scale. So, while in these countries there is a need to continue specific operations and specific investments, there is a tremendous need to examine the overall policy and the institutional environment so that the effectiveness with which domestic and external resources are used is improved.

One of the key issues here is the treatment of the poor in the population in many of these countries who work in agriculture. There has been a general trend toward low agricultural prices and a substantial transfer of resources away from rural areas to urban areas. The so-called controls and subsidies have not, in many cases, been for the benefit of the poor people; they have benefited those who have access to them either through being situated in urban areas or through belonging to a privileged class. We believe that in many of these cases economic efficiency and poverty alleviation have to go hand in hand.

Let me go on now to the issues that arise in our policy dialogue and the prospects for the future.

Clearly, if we are going to have a policy dialogue it has to be on the basis of sound analysis and sound intellectual work. We devote something like 500 staff-years every year to what we call economic policy dialogue, a substantial part of which is actually done cooperatively between the country and the Bank. The fact that we do it with the country leads to a discussion of some of the issues.

Second, economic policymaking is not purely an economic exercise; it is a political and social exercise, and both the countries and the Bank have to be keenly aware of the time it takes to adjust and of the costs of adjustment. This is at best an imperfect science, and its methodology is in many cases not developed.

We also realize that it is for governments to examine the political costs of actions. We, as professionals whose forte is economic evaluation and the experience of various situations that we bring to bear on our discussions, have an obligation to bring out the costs of inaction and the costs of taking inadequate measures, and that is what we try to do. Over a period of time, however, we have had to learn much more not simply about the adjustments but about the framework within which things happen.

There is no rigidity in the way in which the Bank appraoches a policy dialogue, and I might mention two examples of the way in which we have done these things. The first is the case of Indonesia and the other is Turkey.

We have had a continous relationship with Indonesia since the mid-1960s. We established a large mission in Jakarta with some fine economists, and we have kept the staff at a high level. The extent and intensity of our economic sector work in Indonesia are large, and the work covers diverse issues such as agricultural policy, agricultural pricing, credit systems, industrial policy, the financial sector, and transport issues. In Indonesia we have little macroeconomic conditionality in our loans; we make our loans on the basis of the project criteria. The dialogue between the government and the Bank is very effective in the sense that we work closely with them. We take a certain pride in the relation that we have had with Indonesia, and I think that Indonesia takes a certain pride in the way the economy has grown at about 7 percent a year in the past decade and a half. It is one of the fastest-growing economies in the world. It has reduced its dependence on imported food, it has maintained the growth of its nontraditional exports, and it has graduated from a low-income country to a middle-income country in this period.

The second example is Turkey, where the approach was totally different. In the late 1970s Turkey was on the brink of bankruptcy and there was a serious economic crisis. We started working with Turkey at about that time, and we have worked with them through a series of five structural adjustment loans. This has been the most continuous relation that we have had with any country. In the process Turkey has come a long way in the rehabilitation of its economic policy and its structure in terms of use of resources, in terms of exports, in terms of domestic mobilization of resources, and in terms of developing the reform of the state enterprise sector, so much so that when other indebted countries had a severe crisis Turkey was not affected as seriously as were others.

I should like to say that, unlike the Fund, the Bank operates on a very broad front. We do not think that we have quick answers to the situation or that there can be quick mathematical solutions. The focus in our relationship is much more on policy and institutional changes. This also means that not only should we try to improve the quality of our intellectual work and our relations with these countries; we also need a certain humility. Each case is different, each country is different, and the circumstances and the issues in which they operate are different. Therefore, not only do we have to bring to bear on these issues a high quality of experience and talent, but we also have to use a great deal of sensitivity in the process.

Discussion

A speaker began by welcoming the Bank's recognition of its need to learn more about the operation of SALs. Since it now seemed likely that conditionality was here to stay, he said, it was important that its effectiveness be extensively monitored through research on the underlying circumstances of each country and on the effects of the policies imposed by conditionality. This would, it was hoped, over time enhance the ability to design appropriate conditionality packages. He noted that conditionality, when explained in general terms, sounded mild and reasonable, but it seemed harsher and more controversial when the actual conditions became more precise and detailed. Excerpts from two documents—a book on the World Bank by Robert Ayres (1983) and a recent newspaper interview with Zambian President Kenneth Kaunda—were quoted to illustrate the point. According to Ayres (p. 240), "The Bank's first two structural adjustment loans to Turkey, for example, covered sixteen separate areas of macropolicy. Of the Bank's first twelve structural adjustment loans negotiated since the policy was approved, ten included provisions on agricultural pricing policy, eleven included measures to increase export incentives, ten called for revision and review of the entire public sector investment programs, and eight were aimed at the ability of the countries to mobilize resources through changes in budgetary policy."

It was suggested that a quotation from the Kaunda interview might be "something of a consolation" to the Bank: "[the IMF's conditions for its loans to developing countries are] terrifying and . . . aimed at destroying parastatal organizations and raising political tensions. It is like a doctor who prescribes the same treatment for every illness and expects to see results within a year of imposing its harsh regime, but it has not been successful anywhere. In contrast, though the World Bank sets difficult conditions for its loans, they are well thought out and cover a number of years." The speaker sought more details on the actual provisions of the SALs cited by Ayres and on the similarities and contrasts between the conditions imposed by the Bank and the Fund.

Several other questions were posed in the same vein. What happened when the Bank and the Fund were both operating at the same time in the same country? How did the two institutions view the use of the Fund's Compensatory Financing Facility (CFF) as a means of mitigating the effects of collapsed commodity export prices, in lieu of imposing tough SAL conditions on countries whose economic difficulties stemmed from such collapses?

It was in this context of questions and comments that the following points were made. It was too early, said Mr. Husain, to draw general conclusions about the effectiveness of most of the Bank's dozen-odd structural adjustment loans. With the exception of the series of SALs to Turkey, which could be deemed a success because sufficient time had elapsed to permit meaningful evaluation, the returns were not yet in on most such loans. Preliminary indications, however, were that in three cases extensive policy changes had been wrought by means of the SALs and were having a positive impact on economic issues, while in three other cases inadequate design of the SALs or insufficient commitment by the governments concerned had led to problems.

It was argued that the issue of conditionality had to be seen in the context of the extremely difficult situations in which it arose. Countries were seldom interested in undertaking economic adjustment measures when they were flush with money; consequently, these adjustments ended up being more painful because they were made when times were tough. The real question facing the Bank was how to deal with those cases. For example, how should it proceed with poverty-based lending designed to get money to smallholders in a country where the entire power structure was hostile to that goal and a project concept was therefore being corrupted? Or, how could the Bank make African governments realize that the import intensity of their development strategy was unsustainable, given the present picture on aid and on trade?

On the subject of collaboration between the two Bretton Woods organizations, the point was made that certain formal responsibilities were allocated to each and that these were unlikely to be transgressed in public discussion. The Fund was clearly responsible for negotiating the macro framework for fiscal and monetary policy and for exchange rate systems; the Bank dealt with substantive supply-side measures. Disagreements between the Bank and the Fund were not generally made public, as this would be counterproductive, but they did occur during extensive ongoing discussions at the working level. The respective responsibilities of the Bank and the Fund were, however, complementary. When a country faced an economic emergency, it had to begin by establishing a broad macro program with the Fund that enabled the country to utilize its Fund-held reserves in the short run. Thereafter it could seek the Bank's help in building up its capacity for discipline in adhering to a policy framework in the medium and long term.

Bank-Fund policy complementarity was illustrated by reference to public corporations. The speaker stated that, notwithstanding the long-held beliefs of radical development thinkers, parastatals in country after country were hemorrhaging the supply of savings both in total and in the public sector. This issue was dealt with, in the first instance, by the Fund through negotiation of an appropriate financial program and, in the second instance, by the Bank through negotiation of a program to improve the efficiency of the public enterprises or organizations. The Bank's structural adjustment lending had to focus sharply on the general policy framework within which the parastatals operated (for example, their relationship to the central government) as well as on the specific management problems of particular agencies. It was in this manner that the Fund and the Bank were trying to get more discipline into the parastatals' operations from the point of view of demand management in the short run and greater efficiency in the medium and long run. Similarly, in the critical area of agricultural pricing, the Fund's concern was to reduce the subsidy bill in the short run by pushing up the price of food, while the Bank's objective was to build up the government's technocratic capacity to examine agricultural pricing issues in a serious and disciplined way and to formulate appropriate policies. Thus, the Bank was involved in a process of giving discipline to policymaking, not in imposing leverage in a crude sense. Indeed, where SALs had attempted to impose leverage, they had typically failed because of the absence of a national commitment to economic adjustment.

According to another speaker, collaboration (or the lack of it) worked both ways: a Fund program could be ineffective if there was not adequate collaboration with the Bank to put in train complementary policy changes and programs. The example was given of exchange rate devaluations carried out under Fund programs. One purpose of such devaluations was to change the terms of trade for agriculture, both domestically and internationally, but that purpose would not be achieved unless other complementary effects necessary for the success of the price change were brought about through Bank programs.

What if there was no meeting of the minds between the Bank and the country? Mr. Husain pointed out that the Bank (IBRD), as an institution that lived on borrowed money and created debt in the process of assisting countries, had to face two questions. Given the scarcity of its resources, should the Bank continue to lend at the same level in countries where no change was evident despite the existence of substantial opportunities to improve resource use and mobilize domestic resources? And, given that the Bank created debt to be repaid on nonconcessional terms, was it right to do this in countries whose policies already gave rise to doubts about their creditworthiness? Although the Bank recognized that policy dialogue was not something that could be turned on and off at will, it felt that if the dialogue was to have credibility there had to be some relation between a country's economic performance and the amount of Bank lending to it. This accounted for the fluctuations in the levels of Bank lending to individual countries.

A speaker worried about the "sanitized terminology" that permeated the discussion. He welcomed the Bank's reiteration of its commitment to reaching the poor but pointed out that underneath the nonthreatening word "adjustment" and the somewhat more accurate phrase "tough measures" lay the reality of the human costs of the economic difficulties being experienced by poor countries. He asked what had been learned about the negative impact of many of the Bank's megaprojects on the poorest segments of the population concerned. A hydroelectric scheme in India and numerous irrigation programs in Brazil were cited as examples of cases where many thousands of poor people in rural areas had been evicted from their lands without suitable compensation. Noting that conditionality had now become an acceptable term in discussions, the speaker wondered whether in the past the Bank could not have applied some greater conditionality to the governments concerned in regard to such schemes.

Along similar lines, a different speaker commented on the income distribution effects, especially on the urban working classes, of the policy environment being promoted by the Bank. He made several related points: first, changing the policy environment often involved shifting resources toward the rural poor and from the urban working class, whose members were themselves seldom well off. Second, there was an ebb and flow of people between cities and rural areas at different times of the year, reflecting the close family ties that commonly existed between the urban working class and the rural poor. Third, many of the rural poor were women who worked the land, whereas the urban working classes tended to be made up of men. Thus, redistributing income from the urban working class to the rural poor could entail an income redistribution within the family. In this connection, the need for training women in agricultural skills to raise productivity was mentioned. The last point made by this speaker related to the beneficial role that labor unions could play in helping to effect major changes in a country's policy environment, provided that the unions were brought into a rational prior discussion about the issues and were given a chance to make their views known. Perhaps the Bank could encourage a process whereby a shift in resources to rural areas would be accompanied by a related program (for housing, for example) in the urban areas. In the course of its dialogue with member countries, the Bank could suggest that trade unions be included in the consultations. This clearly had not been a feature of the Bank's SAL-based dialogue with Turkey, where the government's attitude toward trade unions had not markedly improved. Success in increasing productivity, the speaker concluded, was not likely to be achieved through suppression of trade unions and abrogation of workers' rights.

Mr. Husain responded that the Bank recognized that there was no way in which adjustments could be made without some losers and some gainers. The governments realized as well that the process of adjustment not only created expectations but also had to take account of the existence of vested interest groups. Thus, adjustments must not be too abrupt. Sometimes this was evident in the rising unemployment and declining real wages that occurred in the wake of some countries' adjustment efforts. But it was a question for debate whether these human costs were a function of the adjustment itself or whether they were instead a function of delayed response to the crises that preceded the adjustment. One view was that the human costs would be far greater in the absence of adjustment.

Commenting that import substitution policies and export promotion policies were being depicted as polar opposites in Bank documents, a speaker wondered whether the Bank ever considered it appropriate for a SAL borrower to impose some level of protection that would enable it to pursue a sensible import substitution policy. He stated that several of the industrializing economies of East Asia, such as Taiwan and Korea, had become successful exporters thanks to the protectionist screen they had erected around their infant industries in the 1950s and the 1960s.

Mr. Husain replied that the Bank was not dogmatic on the issue of trade and protection; rather, its view was that tariffs and exchange rates had to be treated more as issues of allocation and efficiency of resource use than as issues of import substitution or export promotion. Although it believed it was beneficial for countries to take advantage of export markets, the Bank did not deny the justification for protection. In some instances it had assisted governments in streamlining their protective regimes; in others governments had undertaken to reduce protective barriers to improve export incentives or to help existing industries adjust to new circumstances through modernization.

A speaker pointed out that some 73 percent of the failed projects recently identified in a Bank study were attributable to failures in institution-building. He asked whether the Bank was doing anything to strengthen its capacity in this difficult area and added that the Bank and other agencies seemed poorly endowed with personnel trained in the discipline of political science, which was the one most relevant to institution-building.

In reply, Mr. Husain acknowledged that an inadequate or improper institutional focus had indeed contributed to project failure. In many African countries two specific elements could be distinguished in this connection. One was the simplistic and naive assumption that agricultural productivity could be increased successfully by means of enclave projects that were heavily dependent on expatriate manpower. The second was excessive complexity built into a project's design. The Bank was attempting to rectify those shortcomings by making its newer projects less complex and by planning for them to be executed by existing institutions within a country. It was also focusing more attention on manpower recruitment and training and on greater use of local manpower. Internally, the Bank had strengthened its capacity to work on institutional issues by establishing a central unit on public administration to conduct research into and enhance understanding of such issues and also separate units on institutional development within the Bank's regional offices.

Promoting the Private Sector: Should the World Bank Do More or Less?

John Toye
Professor of Development Policy and Planning, University College of Swansea

SYNOPSIS. The role of the private sector has become an issue in aid discussions. The World Bank has formulated a policy on economic development and the private sector, and it has taken actions to stimulate private enterprise (expansion of the IFC, channeling a greater share of IBRD and IDA funds through financial intermediaries to end-users in the private sector, and pursuit of economic reforms designed to maximize public sector efficiency and indirectly to minimize the burden on the private sector). Multilateral aid provides a more consistent long-term approach to private sector development than does bilateral aid. The "crowding-out" problem is negligibly small—and is declining further—in the context of overall aid management problems. Moreover, it is difficult to assess whether countries are altering their choice of balance in their mixed economies on their own initiative or only with a push from the Bank. The arguments that a bloated public sector is really a conspiracy in favor of the private sector and that there is a direct correlation between aid and the politicization of life do not stand up to the evidence.

The Bank and the other aid agencies could play a greater role as catalysts for effective technology transfers from developed to developing countries, and they should not overlook the potential for closer association with nongovernmental organizations (NGOs), which are also part of the private sector. The Bank should not insist on a more thorough liberalization in developing countries than the developed ones are ready to accept for themselves, or on too rapid liberalization, and it should not pursue liberalization on purely ideological grounds.

The way I should like to tackle this topic is by splitting it into three parts. First, I shall give some background on why this particular question has become an issue in aid discussions; second, I shall try to spell out what I understand to be the World Bank's public stance and policies on this question; and third, I shall share with you some reflections on those policies which have arisen from work that I have done in association with Robert Cassen and other colleagues studying aid effectiveness.

Why is the question about aid and the private sector an issue? I had hoped that we would have heard rather more from the radical critics of aid by this point in the symposium so that the remarks I am going to make would have had a more substantial context. Instead, what we have heard so far is a rather modified criticism centered on fungibility. I think that is only one part, and certainly not the most important part, of the kind of aid criticisms which we hear from Lord Bauer and from the parliamentarians and the *Times* leader writers who speak on this issue. Let me try, however, to define the real issue.

It is really a question of "crowding out," that is, whether if you give aid to a developing country and it is used in a public sector project some opportunity for private enterprise is therefore lost once and for all, as it were, by that piece of aid giving. It is the argument that aid goes to feed and fuel a bloated public sector which is really at stake, rather than the question of fungibility. In fact, of course, the crowding-out argument goes rather ill with some versions of the fungibility argument, which says that you do not really know what is happening to aid at all. The extreme skepticism that we were hearing at the end of the discussion of Professor Beenstock's paper was really saying, "Well, we can't tell what the effect of giving aid is because of the fungibility problem."

The issue which I am addressing here presupposes that we do know what is happening to the aid: it is building up a bloated public sector and this in itself is a bad thing because it leads to a concentration of political power in the recipient country; it leads to authoritarian regimes and general political nastiness. Do-gooders, therefore, are contributing to something which, if they realized what they were doing, they actually would not want to do. That seems to me to be the central argument to be addressed.

What is the World Bank's public stance on this question? I recommend those of you who are interested in delving into this to look at a World Bank publication, *Economic Development and the Private Sector* (World Bank 1983a). If I could summarize the policy of the World Bank as it emerges from this publication, and as we have heard it already from Shahid Husain, it is, first, that the World Bank respects the overall framework of public or private ownership which each member government establishes. Second, within that framework it seeks the advantages of markets and entrepreneurship and at the same time it also looks for the advantages to be gained by sound and efficient programs which are beyond the scope of private enterprise in the country concerned. Third, in interpreting the term "advantages," one has to understand it as advantages from the point of view of the country as a whole and not simply, presumably, from the point of view of the private sector of that particular country. It has to be a national judgment.

That is the statement of policy. Notice, incidentally, that the word "equity"—fairness or social justice—is not present in the public statement of policy. It is, I think, the Bank's position that efficient policies will actually do a great deal to help the poor, and that has been said again today. The extent to which that is true, the extent to which there is no real conflict between efficiency and equity, has rather dropped out of view, I would say, in the Bank's public documents.

How is that public stance translated into specific policies by the Bank? I think it is fair to say that there has been, over the years, an increasing concern by the Bank with doing things which stimulate private enterprise, and this can be shown in a number of ways. I am not entirely clear whether the IFC is within our ambit or outside it, but here you have an example of an organization which has grown in recent years, grown very rapidly indeed, and its role is to catalyze private finance and bring private finance into operations in developing countries where, without that catalyst, they would not occur. So that is one clear commitment to the private sector.

The second is within the IBRD and IDA funds themselves, where an increasing share has been directed to final users who are in the private sector. This has been particularly true as the Bank has extended its funding operations to small and medium-scale enterprises and to farmers in the rural sector through various forms of financial intemediary. But even with all of the growth that has come from directing more of the funds to final users in the private sector, something like 80 percent of these funds still end up with final users in the public sector. This fact gives a certain amount of grist to the mill of those who want to run the "aid leads to a bloated public sector" argument.

If you break up that 80 percent, you find that probably about 40 percent of it is going for general infrastructure such as roads, transport, energy, communications, water, urban services, and so on. Another 25 percent is going to agriculture, but through things like irrigation schemes in the public sector, area development projects, and so forth. So the argument has to be that this infrastructure is, first of all, regulated in such a way that it operates in a manner which is helpful to private enterprise and not, as it were, as a burden on the private enterprise of the country concerned. It must be actually assisting it. To ensure that that is so, the Bank pursues, through its sectoral policy dialogues, the set of economic reforms which has already been discussed at some length and which I do not at this point want to go through again. They concern such things as the reform of public enterprise management and the general environment of the exchange rates, interest rates, and tax systems with which the private sector has to cope.

Let me turn now to my own observations on the original argument and on the World Bank's stated position. My first comment is that it is interesting in this connection to make a comparison between multilateral and bilateral forms of aid. I think there is an important distinction here in the way in which these forms of aid address the problems of the private sector. The difference is this—and it is a comparison or contrast which seems to me to favor multilateral rather than bilateral aid, contrary to the people who are now arguing very vociferously for increased bilateral aid because it is in some sense better, or we can be more accountable to Parliament for it. (I think that is the argument that the *Times* is currently running, that it is very important to be accountable to Parliament, that one must always tell the truth to Parliament about everything [laughter], including the aid program, and that it is easy to achieve that with bilateral aid.) My view is that the World Bank has actually been much more consistent in its policies toward the private sector than the bilateral aid agencies. The bilateral aid agencies seem to have swung violently over a period of about fifteen years, from a time when they were engaged in competing with one another to finance public sector steel mills, for example, in India in the early 1960s, to their position now, when they are ultra-private-enterprise in orientation. I think that contrast bears out the argument that multilateral aid provides a much more consistent long-term approach to private sector development than bilateral aid does. I think that is an important fact. It also suggests to me that a lot of the criticism of aid as leading to a bloated public sector should not be directed to the World Bank and other multilateral institutions but rather should be laid at the door of the very agencies which are now, as it were, frothing at the mouth to support private enterprise.

The second thing I want to say about the crowding-out problem is that, whichever way you look at it, it is very small and almost negligible among all the problems of aid management that we have talked about. I am apologetic, really, for talking about a problem which is, in fact, so insignificant. But let me explain to you why I think it *is* an insignificant problem.

A lot of heat in this discussion is generated by the fact that there is no agreed definition of what constitutes a mixed economy. We arrived at this position after debating Stuart Holland's contribution, when we all agreed that it was really the exact mix of a mixed economy that was the key issue and not capitalism versus socialism. However, let us take the view that the United States has got the ideal mixed economy—and we all know that is true [laughter]—that the balance of functions between the government and the private sector in the United States is ideal and optimal. If we then ask how much multilateral World Bank aid has gone, over the years, to institutions in developing countries which are in the public sector in those countries but which would be in the private sector if they adopted a U.S. division of functions, the answer is about 6 or 8 percent. Only 6 or 8 percent of all multilateral funds have ended up in uses in developing countries which are in the public sector there but which in a U.S. framework for dividing functions would be in the private sector. I do not think this amounts to a large problem of aid management.

I would also think, third, that it is a declining problem. It is a problem which characterized the 1960s and 1970s, and therefore a lot of the criticism which is now becoming very fashionable in political circles actually relates to a situation which has by and large passed away. I suppose this is inevitable, always to be condemned to be wise after the event, because the owl of Minerva flies at night, at any rate according to Hegelian ornithology. We are now compensating for sins which were committed ten or fifteen years ago and, in my view, overcompensating for them.

What about the World Bank's stated policy objectives? Are we to take these exactly as we find them? Is practice completely in line with what we are told the official policy is? I find it very difficult to answer that question. The problem revolves around the question of whether the door that the Bank is knocking on is open or half open, or whether there is really a foot behind it against which you have to push. Those kinds of relations do not emerge easily into public light. What one can see is countries altering their choice of balance in the mixed economy. One can see that happening, and one can see the Bank being very involved in that process, but exactly whether the door was open or whether it was pushed is something which I cannot determine. I think particularly of the case of Bangladesh and the changes in the marketing of agricultural inputs there which have taken place in the past few years. A public system has been dismantled and a private system instituted instead, but whether it was the government of Bangladesh that was so keen to introduce this or whether their feet were being gently propelled backward by pressure from our metaphorical door is something on which I would not want to pronounce. The honest answer is, I do not know.

There is an alternative criticism of aid, from the Left, which I think we ought to look at, which is that the bloated public sector is really a conspiracy in favor of the private sector. The argument goes that money is pumped into infrastructure projects, leading to lower prices for the output of the public enterprises, and what this does is to feed the profits of the private enterprises of the recipient country and produce precisely the kind of inegalitarian distribution which the Bank is supposed to be concerned about. I think that argument also needs to be looked at.

If one looks at it, it is superficially pleasing, but I think that in the end it has to be rejected. The reason is that to have a system of artificially low public enterprise output prices is not an unambiguous benefit for the private sector. It sounds so—surely cheap electricity, cheap power, cheap ports, and cheap railways must be good for private enterprise?—but it is not. Why it is not has been well explained by the Bank's economists. If you have excess demand because of too low prices, it is necessary to have some other nonprice system to regulate who gets what, and the other system that comes in to regulate distribution between priority users is often bad news for private enterprise and may well stifle the dynamic expansion of private enterprise in that country. So I would support the Bank's normative argument that genuine pricing and policy reforms are needed if one is going to get a dynamic private enterprise in these countries.

The last reflection that I want to make on aid and the public and private sectors is on the question of the so-called politicization of life, which is said to be the bad political effect of aid. One can look at this within the framework of a number of case studies, and if you do that I think you will find that it is very difficult to establish. There are countries which rely heavily on the public sector and which control the private sector to a considerable extent, but these forms of economic dirigisme predated the arrival of World Bank aid. There was bilateral aid, but—to take the case of India—it is clear that the whole apparatus of which Bauer and company complain was already there, more or less, before the World Bank set up the Aid-India Consortium in 1958. What has happened since then is that under Bank leadership there has been a slow process of dismantling which has increasingly speeded up the process of liberalization that has gathered momentum in the 1980s. There was a similar story in Bangladesh, where the social and political deformations complained of by critics of aid essentially predated the arrival of aid. So it seems to me to be a mistake to suggest that aid has created these things.

At times, aid, having decided to enter a country which has such conditions, does bolster and prop them up for a while, but it is usually the case that there is a transition, maybe a slow transition, and generally the apparatus of control is eroded in some way or another. And, of course, there are plain contrary cases where the apparatus of dirigisme was dismantled precisely in order to acquire multilateral aid; Korea is a good example. The period of heavy bilateral aid in the 1950s underwent a transition in the early 1960s precisely because the American aid agency—the Americans generally—wanted to plug Korea into multilateral lending and knew that they would not be able to do that if they did not get rid of some of the economic controls that existed at that time. That was the conjuncture at which the exchange rate was reformed in Korea.

I want to talk, finally, about some opportunities and dangers—opportunities for further development of help for the private sector via the World Bank and, indeed, the other aid agencies, and some of the dangers that seem to me to be inherent in the current situation.

I think that there is still a major problem in technological transfer from developed to developing countries. This is particularly acute at the level of smallish or medium-size industries. It is much easier for multinationals to transfer and control the transfer of technology than for technology to be transferred to small businessmen in developing countries. We have evidence from a number of studies that this is a genuine problem. Technology transfer agreements which are made at arm's length, as it were, between small businesses in developing countries and business in the developed countries frequently break down, and the technology, in the end, does not get transferred. That is an area where I would like to see more catalytic work being done by the aid agencies to find a way of overcoming this particular market imperfection.

Another opportunity is in the field (which has begun to be explored) of nongovernmental organizations. When we speak of the private sector, it is not simply the profit-making private sector with which we should be concerned. It seems to me that a lot of the virtue of the profit-making private sector is also found in the nonprofit, nongovernmental organizations that operate in developing countries. I wonder whether enough has been done by the Bank to relate to those. I wonder whether it is not rather mesmerized by the notion that working with the private sector is a question of finding businessmen who have to make profits. I do not think that the private sector is like that, and I do not think that getting its advantages for the developing world requires us to think profit *all* the time.

This leads me to a brief list of some of the dangers I see as inherent in the situation. One of these is that the Bank is in danger—I think it is a danger which it actually appreciates quite keenly, but which may lead to difficulties for it in political terms, at any rate—of insisting on a more thorough liberalization in the developing countries than the developed countries are ready to accept for themselves. There is an asymmetry here in insisting firmly on liberalization in developing countries when the trend of policy in developed countries is running in the opposite direction, toward protection, toward inventing new and cleverer forms of protection. That was really the thrust of my question to Timothy Raison in the discussion about the extent to which certain schemes which are part of bilateral aid programs are actually a form of disguised protection. All of that is going on at the same time as we are urging the World Bank to press developing countries harder to open everything up. I think that that is a stand which will be politically difficult to sustain in the long run, quite apart from the moral injustice of it.

Second, there is a danger in trying to do everything too fast, or wanting to do it too fast. The best liberalizations are slow liberalizations, and two admirable features of the Bank's activities are its continuity and its ability to learn. Those two merits must be applied in the prosecution of liberalization. Do not do it in the way in which it was done in India in the middle 1960s. Do not do it in the way in which it was done in some of the countries of the southern cone of Latin America in the 1970s.

The third danger is that liberalization can become an ideology and be pursued for ideological reasons. This is something that worries me considerably. It is also what obviously worries a number of people here. The fact that the name of Bela Balassa has been on a number of lips does not surprise me in the least in this connection because it seems to me that the arguments of Balassa about liberalization are highly ideological arguments. If you examine the intellectual foundation on which they rest, you will find that it is flawed, even in terms of the standard economic theory of welfare and distortions. What Balassa is doing is arguing for the removal of all policy-induced distortions in a world in which there are also a lot of endogenous distortions. I am using the language of Jagdish Bhagwati here, for those who want to read the texts, the neoclassical sacred scriptures. You cannot simply insist on the removal of policy-induced distortions if you are not at the same time addressing the endogenous distortions of the economy, because there is no guarantee that you are going to arrive at anything called "optimal welfare" if you do that.

I am not saying, you will understand, that a lot of the practical measures that have been taken by the Bank are not sensible and good. What I am saying is that the way in which they are defended is in fact a flawed defense, an ideological defense, and there is a real danger that the Bank will not be able to hold back from climbing on the full gospel, free-enterprise Manchester liberal bandwagon. I think that if it did that it might gain some short-term advantages, but the continuity and consistency, the ability to learn, which are the life blood of the Bank, would be very seriously threatened.

Discussion

No clear theme emerged in the discussion of this topic, as participants commented on various aspects of the presentation. A speaker posed the following series of questions. Were the Bank and the other aid agencies striking the correct balance on the degree of support they gave to the public and the private sectors, respectively, in the developing countries? Did those operating in the private sector in developing countries feel that crowding out was occurring? Did they favor greater liberalization or greater protection? Did they prefer to see the Bank concentrate its efforts to influence policy on elimination of distortions or on some form of incentives to private sector enterprises?

A speaker identified three factors that had, in his view, led the aid community to de-emphasize, in the years since the end of World War II, the role that it should play within the private sector. One factor was that, as most bilateral and multilateral aid was government to government, it was administered by civil servants who were most familiar with and most comfortable in a public sector environment. A second factor was the sheer practical difficulty of working with the private sector: how did one deal with a multitude of small entrepreneurs in the context of a $50 million or $60 million Bank loan? Finally, the political connotation of the phrase "private sector" made the World Bank and the bilateral aid agencies shy away from any big push to increase their lending to the private sector; indeed, the underlying assumption seemed to be that giving money to the private sector would crowd out the programs for poverty alleviation which were the main focal point of aid. He argued that if a country had a mixed economy, the aid community had a role to play within the private sector; the nature and size of that role would, however, be up to the recipient government to decide.

In response, Professor Toye dismissed as insignificant the fact that aid was government to government. It was the things that happened after the aid check was handed over, as it were, that should be highlighted. However, he conceded that the problem of "dealing with 100,000 entrepreneurs" was indeed acute. The Bank had tended to use financial intermediaries such as national development banks to take on that task. Although that strategy had not been entirely successful—some repayment problems had occurred, and some institutions had turned out to suffer from serious weaknesses—much progress had been made in the past decade and a half. The Bank had evidently learned from its past experiences and was devising better ways of developing institutions capable of channeling aid funds to many individuals.

If one disagreed with the Left's proposition that public sector enterprises which ran massive losses were basically providing a hidden subsidy to the private sector, a speaker asked, how did one assess the relation between the public and private sectors where such massive pricing distortions did not exist?

Professor Toye replied that pricing systems, rather than the relative mix of public and private enterprise, were the relevant issues in this context. Even with a heavily public sector-oriented mix it was necessary to have a pricing system that functioned properly. No contradiction was apparent in socialist thinking which divorced those two things.

A speaker postulated the thesis that development projects had to be based on assumptions of much lower notional financial returns than those yielded by private sector investments. His reasoning was that all economic activity involved capital—which is what a bank provides—as well as labor and land, which seldom got as much attention as the first input. By definition, where development was most needed, the resources generally were least available. Therefore it was likely that, with limited inputs of capital, returns on labor and land would be lower than elsewhere. If an organization responsible for that input of capital were going to take its norms from the returns obtainable in New York, London, or Hong Kong, it stood to reason that there would not be much activity where resources were minimal. This indicated to him that, irrespective of whether resources were channeled to the public, private, or intermediate sector, a much lower notional financial return had to be accepted and some type of economic bulkheads to ensure that the total value of the returns to the community was not dissipated had to be included in the conditions.

The issue of asymmetric liberalization that had been raised in the presentation was brought up by a speaker who asked the audience to imagine a situation in which the U.S. government was about to request a stand-by from the IMF. He was sure that in such a case the Fund would regard the United States as its most delinquent member, what with its huge budget deficit, overvalued currency, massive public spending on nonproductive sectors such as defense, overproductive agricultural sector that was unresponsive to market forces, and increasingly protectionist attitudes. These policy features, which were being pursued by the one donor that was giving advice to the Bank and the Fund on adjustment programs for borrowing countries, certainly put into perspective the problem of asking developing countries to do more than the developed countries themselves were willing to do.

Two speakers made the point that it was inaccurate to depict only two economic sectors, the public and the private. In fact, there was a third one made up of non-profit-making, nongovernmental organizations such as trade unions, private charitable agencies, and cooperatives. According to these speakers, the existence of this sector both in donor and in recipient countries was directly relevant to the Bank in several ways. For one thing, the Bank would have to demonstrate that its basic needs strategies were in line with some of the objectives being pursued in the developing world by the nongovernmental sector whose support the Bank was seeking. In addition, the Bank might usefully examine the type of cofunding and joint initiatives being undertaken by bodies such as the European Commission with nongovernmental organizations. Also, the Bank should perhaps distance itself from the Fund when the latter acted on purely economic criteria without due regard for complex and volatile political factors, as it had done in Turkey and appeared to be doing in Brazil. Another aspect of the nongovernmental sector's importance was to be found in the role being played by the self-governing peasants' cooperatives now in charge of China's agriculture within the overall socialist framework of state planning. As this approach would surely serve as a model for much of the rest of the developing world, the Bank ought to study it carefully.

The subject of direct private investment in developing countries was discussed by several speakers. One described the principles that a proposed code of practice to facilitate such investment might contain: freedom to employ expatriates with special skills; freedom to repatriate a reasonable share of profits; absence of penal taxation on profits or on employees' salaries; guarantees against nationalization or expropriation without full compensation; no insistence on 50 percent minimum equity participation by host governments; application of the code to all existing private sector firms; and agreement in advance on procedures for settling disputes. This speaker felt that endorsement by the Bank of these minimum requirements for any investment, such as by the IFC, for example, would help developing countries enormously in attracting private investment. In response to a query he added that political risk insurance, while not a prerequisite, would certainly be helpful. A different speaker thought it essential to add another requirement to this list: that private foreign capital not be given any subsidies by the domestic economy nor be allowed to hold monopoly power.

Professor Toye singled out the principle of equal application of the code to all existing private sector firms as the crucial one. He stated that it was the practice of many developing countries to offer identically bad terms to foreign investors as existed for their domestic private investors. This had been the case in India in 1948, for example. Were such countries to provide the other conditions stipulated in the proposed code to attract private capital, they would actually have to discriminate in favor of foreigners—clearly an impossible course to follow in political terms. Thus it appeared that this code of conduct would stand a greater chance of success in those countries where the regime for domestic investors was being reformed along the lines being suggested by the Bank. As developing countries proceeded with such reforms they would gradually reach a point at which they could satisfy the requirements of foreign private investment without having to discriminate in favor of it.

Another speaker questioned the merit of exhorting developing countries indiscriminately to embrace foreign investment. He pointed out that much foreign investment was concentrated on a small group of countries and added that "what is worse than being exploited by a multinational is not being exploited by a multinational." He asked what role the Bank could play in trying to encourage foreign investment in a broader spread of developing countries and what practical measures the Bank considered feasible for countries to adopt to attract foreign capital. He concluded by wondering whether it was indeed possible for developing countries to do this successfully or whether the Reagan rhetoric would instead persuade countries to take actions that were detrimental to their own interests.

On a different subject, a speaker observed that people from organizations such as the Bank sometimes encountered cultural difficulties when confronted with entrepreneurs in developing countries: they did not speak the same language. He wondered what the experience of the IFC had been in this regard. Another speaker also asked a number of questions concerning the IFC.

An IFC representative replied that the IFC's experience was that its own investments mobilized additional flows of capital between four and six times greater; for planning purposes, however, the IFC assumed a lesser gearing ratio, about four to one. It was accurate to say that $7.5 billion of the IFC's own capital invested over five years would generate about $30 billion worth of projects. Also, the IFC had observed that public sector investments financed by the Bank and others provided important markets for domestic private enterprises. Indeed, a sustained public sector investment program, such as in power or water, was critical for a reasonably thriving private enterprise segment. He noted that the IFC's disbursement level amounted to only about 6 percent of the Bank's disbursements, but the relation of disbursements to direct commitments by the IFC was consistent with that for the IBRD and the IDA. As for the IFC's expanded program of activity, it was likely to include an energy exploration program, emphasis on Sub-Saharan Africa, emphasis on restructuring ailing companies, and greater involvement in development of national institutions such as venture capital companies, risk capital funds, and whatever would help raise domestic savings levels.

The comments about IFC prompted Professor Toye to point out an ambiguity at the very core of the discussion on how to promote the private sector. That is, whose private sector was being discussed, that of the developing or of the developed countries? There was a conflict of interest between these two, and serving one by no means necessarily served the other. Much donor policy was "getting itself in a knot" because it was not clear to whose interests it was catering. In his view the Bank and its affiliates on the whole did more to serve the private sector of the developing countries than did bilateral aid, which was bending over backward to serve the interests of the donors' private sectors.

Reaching the Poorest: Does the World Bank Still Believe in "Redistribution with Growth"?

E. A. Brett
Lecturer, University of Sussex

The chairman introduced the session by reading three quotations from Ayres (1983), with the hope "that one of them turns out to be the appropriate text."

- "The concern that the Bank might desert the poor must depart from a realization that under McNamara it never totally embraced them" (p. 235).
- "While McNamara's Bank had for some a 'leftist' image which obscured the real nature of its operations, Clausen's Bank has acquired for others a 'rightist' image which likewise obscures what the Bank is really doing" (p. 238).
- "If there is any betrayal of the poor on the part of the Bank, now or in the future, it is seen by this study to have its roots in the international and national conditions under which it must operate, not in the policy designs of McNamara's successor" (p. 255).

Dr. Brett then made his presentation.

SYNOPSIS. The publication by the World Bank of *Redistribution with Growth* (Chenery and others 1974) marked a watershed in the transition from orthodox development theory, with its conception of the irrational traditional farmer as opposed to rational bureaucrats and large-scale entrepreneurs, to the conception of the rational peasant. The new approach made it possible to link redistribution and growth.

The Bank's accomplishments with poverty-oriented programs devised during the McNamara era were praiseworthy, but there should be no complacency about the plight of the world's poor. Three issues arise about the Bank's capacity to put into practice its continuing commitment to redistribution with growth. The first point concerns the significant ideological contradictions in the Bank's current thinking on macroeconomic issues. The unsympathetic attitudes toward redistribution with growth now held by the senior people in the Research Department could have a negative effect on the Bank's economic policies. Of particular concern are the areas of trade liberalization and foreign private capital, which should not be given subsidies by the domestic economy or be allocated monopoly power.

The second issue is that of political constraints. There exists in developing countries a political class that benefits directly from monopoly rents and subsidy structures and that therefore has a vested interest in maintaining the status quo. The problems are also induced by the procurement policies of aid donors. The policy problems that have arisen and the ensuing policy debate are being skewed toward a coming to terms with reactionary elements of the ruling classes in developing countries.

As for the third issue—that of constraints on administrative delivery systems—no adequate bureaucratic theory is available to help tailor effective and appropriate inputs into public sector management processes, and the Bank itself is constrained by its own bureaucratic structure from getting through to small farmers and other impoverished people. The Bank should acknowledge the structural problem, reappraise the whole socialization process of bureaucrats and others, and explore using such alternative structures as nongovernmental organizations and cooperatives to get resources to the poorest.

I think that the three sentences quoted by the chairman, and the implicit problems and contradictions in them, both at the level of what the Bank is doing and, more especially, what the Bank is seen to be doing by outside observers like myself is simply a useful way of leading into a discussion of an area where, it seems to me, the contradictions are rife. These contradictions are rife in terms of the intention and much more in terms of the possibility of putting intentions into practice. My concern is going to be to try to focus on the latter set of questions. I might start by saying that, with your indulgence, having sat through much of the discussion, I now have to change the title of my talk. My title was, "Does the Bank Still Believe in 'Redistribution with Growth'?" We have had, I think, a very clear and welcome statement from senior members of the Bank that they do, and I, for one, am quite happy with that assurance. So my concern today is not going to be, "Does the Bank still believe in 'Redistribution with Growth'?" but "Does the Bank have the capacity to put that intention into practice?"

May I start with a brief historical review of what seems to me to be the change in the intellectual context with which I am concerned? In 1974 the Bank published a major book—I think it is one of the important classics in development theory produced in the postwar period—*Redistribution with*

Growth, by Hollis Chenery and others, a work which followed from the pioneering work done by a series of International Labour Organisation (ILO) missions, particularly in Kenya and Colombia. The Institute for Development Studies (IDS) played an important role and was also heavily involved in the discussions that went on before publication of *Redistribution with Growth*, in which essentially a kind of reversal in development theory took place.

If we look at the old import substitution-industrialization orthodoxy, we see a kind of implicit model of the developing world which divided it into a formal sector and a traditional sector. The formal sector was that rational world of informed bureaucrats and large-scale entrepreneurs who were capable of making rational decisions, capable of organizing modernization, capable, therefore, of bringing those countries into the modern world and taking them out of their traditional backwardness and incapacity to produce. The informal sector—that is, the other half of the dualist model—was composed of traditional individuals who were incapable of responding rationally to incentives, who were incapable of producing rapid production increases, and whose fate was to be a gradual, and, it was hoped, painless, extermination along the lines suggested by Arthur Lewis in his classic article on economic development with excessive supplies of labor (1954).

It seemed to me that *Redistribution with Growth* inverted that model. The people who went out in the early 1970s confronted a situation of massive structural problems associated with growing levels of unemployment and underemployment that arose out of what they saw to be, on the one side, irrational bureaucratic decisionmaking and, on the other, the irrationally capital-intensive structure of large-scale industry. As a result they arrived at a model which by implication asserted that it was in fact these so-called modern structures with their dependence on Western technology and Western models that constituted the obstacles to development, and that it was in the traditional sector, where the small peasantry and the small entrepreneurs, artisans, and so on were, in fact, saving the poor from actual starvation, that the most rational use of resources was taking place.

Indeed, I think that here the conception of the "rational peasant," which Michael Lipton pioneered, is the crucial notion, and that the transition from the conception of the irrational traditional farmer in the 1950s and 1960s to the rational peasant maximizer of the 1970s and 1980s was a crucial watershed in the way that we approached the problem.

For those of us on the Left who are more concerned with a development process having positive equity features than massive growth features—and, as a South African, coming from the most dynamic economy on the continent, but witnessing the kind of squalor and degradation that can be created where those concerns are not up front in decisionmaking—that transition in development theory was a very welcome and helpful one because it made it possible for people who were committed to an egalitarian structure to argue the possibility of linking those two words, "redistribution" and "growth." As one who considers himself to be on the Left—although not all my comrades in the Labour Party would agree with that position—I was more committed to and more wedded to that theory than to the subsequent emphasis on basic needs. Although we all accept that the basic needs of the poorest are something we have to be concerned about, I would argue—and I think most people in the Bank and the Fund would agree with me—that the possibility of meeting basic needs is a function of generating genuine productivity increases among the poor. I think the notion that somehow basic needs are something that people have a right to, whether or not they produce, and that somehow external charities can be brought in to resolve those problems is not a viable long-term option. What we have to consider carefully, therefore, is the extent to which we can, through mechanisms that exist at the international level and, more especially in this context, through the mechanisms which the Bank has at its disposal, generate a transition, in policy and administration, that can make that process of generating a genuine productivity dynamism among the bottom 40 percent a reality.

Talking at this stage of the conference does have some disadvantages because this issue has been taken up and statements have already been made by the Bank that to some extent answer the questions that I am going to ask. I would like, however, to take the time that is available to try to raise a series of relatively sensitive issues, some of which have been glanced at and commented on, and to try to spell out what seems to me to be a set of problems with which we have to deal.

Historically, I think it is fair to say that the acceptance of—let us call it the McNamara orientation—has had real effects. There has been a massive expansion in investment in agriculture with, I think, at least an attempt to get resources to peasant agriculture. There has been a willingness to experiment with nongovernmental organizations and a much more recent phenomenon, a willingness to address the problems of the landless; a rejection of heavy subsidies to the formal sector—an emphasis on viable exchange rates which do not subsidize capital and capital intensity at the expense of labor intensity—and an attempt to at least deal with the problems of small-scale industry, small-scale workshops, and the investment in social and educational infrastructure which is necessary to upgrade the productive capacity of the poor. I was talking to Michael Lipton earlier, and when he was at the Bank he did a calculation which argued that the percentage of the resources put into poverty-oriented programs increased to 30 percent from 6 percent during the decade 1972–82. Now that is very welcome, and therefore I am putting my points in a way which is not going to be very critical of the Bank.

I am impressed by the extent to which the Bank has taken the lead in this respect. Personally, I consider what the Bank has done—in comparison, particularly, with what the ODA in this country is doing at the moment—to be something that we should be emulating. I do not think, however, that we can sit back and say that what has actually happened to the poor in the developing world over the past decade or decade and a half can be a source of complacency to any of us, the Bank included. I suspect that the population now living in absolute poverty in the world is probably 1,000 million, and that all of us sitting here in these rather elegant surroundings, and having had very welcome hospitality from the Bank have to take that situation seriously.

First, let me say that the evidence suggests that the poverty-oriented process and the emphasis on raising the productivity of the poor do not necessarily involve any reduction in growth potential. In response to a point that was raised earlier, let me read you a paragraph from the World Bank's *Ninth Annual Review of Project Performance Audit Results* (World Bank 1983c, p. 34) concerning evaluation of agricultural performance:

> Poverty-oriented projects were cost effective, socially equitable and economically viable. They were much smaller in size and only half as costly as other agricultural development projects. Poverty-oriented projects were most outstanding in their expectation of achieving food production targets and in reaching a large number of beneficiaries. Even though they accounted for only a fifth of total project costs in this year's group, they were expected to generate a third of the total incremental food production. Audit estimates of food production from these projects were at levels substantially above appraisal projections in most cases. Project cost per beneficiary was considerably lower than for other agricultural projects, confirming the findings of previous Reviews even though a slightly different concept of poverty target group has been used in this Review.

Two points are important here. The first is that—in relation to the food crisis, in relation to the food gap, the external dependence on food, and thus the foreign exchange costs—the poverty programs obviously performed brilliantly. Notice, however, that only one-fifth of investment took place in those projects—one-fifth of investment for an area in which, one imagines, at least 60 to 70 percent of the rural population would fall into the poverty group. So, although we have a very successful impetus, in terms of potential, we have to ask the Bank whether they are satisfied that a large enough proportion of their resources is going there.

Having said that, I also welcome the Please report (World Bank 1984c) which, it seems to me, in a sense continues this emphasis and recognizes it and, to some extent, moves back away from what I think was a break with that commitment in the earlier Berg report on Africa (World Bank 1981), in which the emphasis on the progressive farmer, the rich farmer, was much stronger.

What I should like to do in the time that remains is to raise three questions which seem to me to bear on the possibility—given the context within which the Bank is operating and given my own understanding of the policy debate which has been going on in the Bank—that the present orientation needs to be looked at carefully. My concern is simply to raise issues which I am hoping that people better informed than I am in the audience will be able to deal with.

These three issues are, first, the question of potential inconsistencies and contradictions within the total structure of the Bank's economic policy with respect to these problems; second, the problem of the political constraints which these problems necessarily run into; and, third, the problem of administrative constraints which seem to be encountered when the policies are put into effect. Let me take these three issues in turn.

We see, at the level of macroeconomic policy and orientation, an IMF–World Bank orientation. The World Bank has a somewhat different position from that of the IMF, but it operates within the same orientation toward adjustment through devaluation, liberalization, and the encouragement of foreign private capital on the one hand and, on the other, the commitment that I have already outlined toward developing a productive potential on the part of the poor. I have yet to be convinced that all of the aspects of the devaluation–liberalization–foreign private capitalist complex invariably and in a noncontradictory way will make possible the further development and expansion of the informal sector. Here, I think that devaluation is the point I would take. I regard grossly overvalued currencies as a mechanism for illegally stealing money from the poor, and I am therefore in absolute accord with the Bank on that point. The question of trade liberalization and foreign private capital, however, is something which does have to be looked at closely in relation to the infant industry argument, because it is with respect to the informal sector—the small producer, the small manufacturing producer, and the small agrarian producer par excellence—that the whole of the infant industry argument applies. This is the one central argument in favor of protectionist and interventionist structures which has been with us from the 1830s. It served as the basis for the development of the economies of countries like Germany and the United States when they were competing on unequal terms, and it now obviously has to be taken seriously.

I am therefore concerned that at the Bank there does seem to be a significant ideological contradiction. The name of Bela Balassa has come up often in the discussion. Deepak Lal and Anne O. Krueger also have senior positions in the Bank and now control the Research Department, which some years earlier had produced *Redistribution with Growth*, and my reading of their texts suggests that they have little sympathy with the view expressed in that book. John Toye has done a brilliant review of Deepak Lal's recent book *The Poverty of "Development Economics"* (1985), and the IDS has produced a critique of Krueger's analysis of the Asian newly industrializing countries which massively undermines her position (Institute for Development Studies 1984). I am therefore concerned that the orientation will be taken to a point where a series of changes will take place that could have negative effects.

Here we also have to take up the question of private foreign capital. I have reservations about the excessive encouragement of private foreign capital. I do not argue that private foreign capital can never make a positive contribution, but in the African context we have to take a number of factors into account. The first is that historically in tropical Africa private foreign capital has invested very little. The number of multinationals that wish to invest in Africa is very small, for good reasons. They operate on the basis of developed technology, and the African markets and the African context that they might want to go into are relatively underdeveloped. The consequence is that it has been necessary for African governments that have taken private foreign capital to make massive concessions to the companies and to provide them with massive subsidies. One of the points about the public-versus-private debate that we have overlooked is the fact that some of the major subsidies arising out of import-substituting industrialization did not go to the parastatals but to private foreign capital. If we look at the Kenyan motorcar industry, built by Firestone in the 1970s and employing about 300 workers, it produced enough tires for the whole East African market and involved massive subsidies while having a negligible and possibly negative effect on employment because of the level of subsidy that was involved.

So, if we are going to plug that commitment into our model, and if we are going to take seriously the points about how to encourage private investment that were made in the last discusssion, I would have to add another requirement to the proposed code, which is that private foreign capital should not be given any subsidies by the domestic economy and that foreign companies should only be brought in when they can establish themselves without net subsidies from consumers. Further, they should not be allocated monopoly power, although in fact monopoly power has normally been one of the conditions under which foreign private capital is invested in Africa, precisely because of the small size of the market and, therefore, the necessity for a guarantee. Without monopoly power, they would not be willing to set up.

The evidence we have up to now is that there are a great many negatives associated with that kind of monopoly foreign private capital. This is a critique not of private capital but of monopoly private capital subsidized by import substitution policies with high tariffs, generating high foreign exchange costs in terms of a massive reliance on imported inputs, a high degree of repatriation of capital, and a large amount of high-cost imported labor.

I am therefore concerned, when I look at the Bank's position, that the Bank recognize the potential contradictions in that kind of way and, when it makes policy decisions, that it come out on the side that constantly puts emphasis on the small-scale producer in the developing world.

The second issue I want to raise concerns the political constraints. The existing structure of subsidies and monopoly rents, which arises out of state intervention in the form of crazy bureaucratic apparatuses like the Ghanian Cocoa Marketing Board (which, I was recently told, employs some 200,000 people), has generated a political class in those societies that depends directly on monopoly rents which accrue to them. Indeed, one can show that a great many of the irrationalities, particularly in the bureaucratic sector, are functional for the maintenance of those elements.

In addition, a great many problems are induced by the procurement policies of aid donors. My own work on agriculture in East Africa in the 1960s and 1970s clearly demonstrated a totally irrational strategy of investment in East African agriculture that arose out of the needs of British industry to sell tractors and other inputs for an inappropriate exotic cattle industry.

There has been some discussion in this conference about the extent to which the World Bank has had to use policy leverage which has had negative effects on particular strata—the urban working class is one which has been mentioned. The defense which has been given to us is that if you are consuming more than you are producing, you have to adjust, and hard decisions have to be made. The point I would make is that it is not enough to put it in a general sense like that.

An interesting point was made in the discussion following Mr. Raison's presentation, when it was asked whether the World Bank was still willing to accept a land redistribution program. If we are, for example, concerned to increase food production capacity, reduce food imports, and increase the capacity for producing agricultural exports, clearly the evidence of the ILO reports and the evidence which I have just given you from the Bank's own project review suggest that small-scale farmers have a much higher propensity to produce domestic consumables, a much lower propensity to consume imports, and a much higher propensity, per unit of land and labor, to produce agricultural exports. Therefore, one mechanism for resolving the adjustment problem could very well be land reform of a massive kind that involves getting rid of absentee landlords with a high propensity to consume Mercedes motorcars and the like and putting small peasants onto the land in their place. It seems to me that if the Bank is going to come to us and say that it is willing to use its leverage for certain purposes—for example, liberalization, or increasing the amount of private foreign capital—then I cannnot see that they can legitimately say that they should not use their leverage for extracting from government a massive land redistribution process which clearly would have major positive effects on the balance of payments problem.

Thus, there is an evasion in what we have now. The policy debate and the policy problems which have arisen have certainly been skewed in the direction of partially coming to terms with internal elements in a ruling class which in my view is in many respects a reactionary class.

Finally, the administrative structural constraints. Here we have a problem. Historically, the emergence of the kinds of structure I have been referring to—the Cocoa Marketing Board, the Coffee Marketing Board, and so on—was a function of an attempt by the state to uphold the interests of particular, rather reactionary, capitalist elements in the colonial period. The structures were subsequently taken over at independence, the expatriate capitalist elements were got rid of, and the bureaucracies have now become a mechanism for the appropriation of monopoly rents from the small peasantry, with devastating costs to production. That part of the analysis which the Bank has produced is absolutely correct, and those problems have to be dealt with. If they are not, we shall get no increase in productivity.

A process of privatization in the sector that generates small-scale production and uses small-scale intermediaries would have positive equity effects and positive production effects. The early colonial history shows that there was a very positive and efficient marketing sector operating on the basis of large-scale processors and small-scale middlemen when that sector was allowed to operate competitively and when the state did not have a monopoly position. Once the monopoly started to be introduced by the state, both the equity and the production effects became much more negative. Simply to assert, however, that the problem is an administrative one of getting resources to small peasants and that it can be solved by total privatization, getting the prices right, educating the farmers in schools, and leaving the rest to the market totally ignores two fundamental problems. The first is that the private sector in those contexts is likely itself to become monopolistic in response to a whole series of traditional power relations which can be and are exploited in direct ways by particular people. More importantly, a major gap exists because for fifty years the whole development of the merchant class—the agrarian class in the peasant sector—has been inhibited by the creation of the bureaucratic structures. Therefore, to assume that a merchant class can come into being overnight without external intervention and help is a dubious assumption.

Thus, we do require a substantial input into the public sector management processes that are associated with getting resources to the peasantry and dealing with development of the agrarian and merchant classes. Here, I think, we have a fundamental problem in that we have virtually no adequate bureaucratic theory that can help us deal with the fundamental structural problems that exist with respect to public sector interventions. Up to now the problem we have had to confront has been that the whole public sector provision was based on Western models dependent on certain political prerequisites which exist in Western countries, namely, effective democratic organization and therefore the enforcement of accountability over bureaucrats. These conditions are absent in developing countries, where the bulk of the population is semiliterate, is out of touch with the media, cannot organize itself, and is therefore likely to be exploited by bureaucrats who are given monopoly powers.

I was going to give you a couple of references. The structure of the World Bank itself was considered in an article by Clough and Williams (forthcoming), "Decoding Berg," in which they stated that the problem is that the Bank itself is a kind of bureaucratic structure which faces real problems in getting through to small farmers. The point was made, "How do you get resources to 200,000, or a million, small peasants when you are a large bureaucratic organization yourself, like the Bank?"

Robert Chambers, in *Rural Development: Putting the Last First*, raises a series of issues about the way in which the socialization process of bureaucrats, agricultural extension agents, agricultural scientists, and so on orients people toward solutions which are not "last first" solutions but "first first" solutions. It seems to me that a fundamental reappraisal has to take place, and this is something that the Bank should be doing. Nongovernmental organizations, cooperative organizations, and a whole series of alternative structures need to be investigated, used, and developed as mechanisms which do not create centralized bureaucratic monopolistic structures. We have used such structures traditionally, notionally, to get resources to the poorest, but in fact they extract resources from them in the form of monopoly rents. I should like to see a clear recognition from the Bank that it accepts that structural problem and that it is going to put its considerable resources to the purpose of dealing with it.

Discussion

Dr. Brett's presentation was welcomed as "a reflective and substantive contribution from a radical point of view" and "a most fascinating contribution." One speaker from the World Bank found himself in agreement with much of what Dr. Brett had said, particularly that the distinction that used to be made between the formal and the informal sectors was not relevant to developing economies. Much of the Bank's work on agriculture recognized the innate rationality of peasants and small farmers. In addition, awareness that a small class benefited from subsidies, incentives, and controls because of its monopolistic position was an integral part of the Bank's efforts, through dialogue, to induce or prod borrowing countries to examine the purposes and effects of such subsidies and controls.

Another speaker drew attention to the sharp criticisms that had been expressed by Dr. Brett and others during the conference about the work being conducted at present in the Bank's Research Department, which is the part of the Bank that tends to relate to people at universities. He hoped the senior Bank staff present at the meeting would report to the Bank management in Washington the clear message that these criticisms conveyed—that the Bank had to make a more vigorous effort "to get its operational people closer to its critics, and to university people in general."

A different speaker took issue with Dr. Brett's conviction that the Bank was indeed committed to redistribution with growth. In his view the Bank was merely committed to the creation of new productive assets with broader control by the poor, but this was not the fundamental and thoroughgoing redistribution of productive assets that the original theoretical framework of redistribution with growth had envisaged, he stated.

In this connection, it was pointed out that only one instance of genuine and autonomous land redistribution had occurred in a developing country since World War II, and that had been in Ethiopia in 1974. It was further recalled that when the revolution in that country introduced land reform the World Bank had doubled its lending program, which it had kept low during the Emperor's regime precisely because of the government's failure to address the issue of land reform. According to this speaker, however, within a few years the lending program was curtailed significantly and ultimately stopped entirely because of political pressures on the Bank "not from a Reaganite or Thatcherite government, but from a Labour government in [the United Kingdom] concerned with the compensation issue in Ethiopia." The British Labour Party, the speaker said, had refused to give the Bank the time it needed to sort out the complex political problems it faced in dealing with compensation in the context of a radical government that was introducing land reforms. As a result, the Bank had been forced to withdraw its wholehearted support for land reform and economic revolution in Ethiopia. Another speaker observed that even though the Bank fully recognized the importance of the small farmer and endorsed the concept of equitable land distribution, there was only so much it could do within the political constraints imposed on it. Insistence by the Bank on proceeding with land reform before anything else might prevent it from doing other things that substantially benefited small farmers and the poor.

Dr. Brett pointed out that perspectives on the question of distribution of assets varied, depending on whether the land-short Asian economies or the land-rich African ones were at issue. His own experience had been in Africa, where the open land frontiers that still prevailed in the early 1970s made it possible for poor peasants to produce without a substantial land redistribution. He was concerned, however, that by now the situation was much less favorable, given the major land grab that had been organized largely by the class of people who had obtained bureaucratic monopolies and were using the monopoly rents they were extracting to buy up land in the rural areas. This pushed the land frontier back and prevented development by the small peasant. Thus, the political process had been aided and abetted by the aid mechanism. He illustrated his point by citing the dramatic example of a land scheme in Angola where $7 million in American aid had been used to create thirty-two large 3,000-acre cattle farms for the benefit of the leading politicians, army officers, and government officials of the district. This had resulted in a zero increase in livestock output and in removal of a huge area of land from access by transient populations that usually grazed their cattle there during certain times of the year. The speaker attributed this type of major and intensifying problem to failure to develop policies for redistribution with growth and to toleration of monopoly rents. He conceded that it would probably not be possible for the Bank "to take this hot potato on board." He could not imagine some of the Bank's leading Executive Directors being very impressed by the Bank's forcibly effecting land redistribution programs. But the central point, in his view, was the redistribution of assets in terms of the availability of such inputs as credit and seeds. The technology already existed to bring real resources and real productive potential to small farmers, but the political will and administrative structures to do so were in their infancy.

A speaker questioned whether the main problem was one of giving the rural poor adequate incentives to increase agricultural output or one of giving them access to the means of production. His understanding was that the Bank viewed incentives as the key in the agricultural sector and was therefore stressing measures to liberalize the market by, for example, dismantling marketing boards. But in his view, access to the means of production, such as land and capital (or credit), was the real issue. He suggested that mechanisms for getting credit to the poorest, who were often not deemed creditworthy, be examined and discussed.

In responding, Dr. Brett rephrased the question as, "Is it resources or prices that determine the possibilities of peasant agriculture?" He added that the answer was "yes," "no," and "yes and no." He elaborated by giving an example. The peasant farmers he had encountered in Uganda over a period of several years owned neither wheelbarrows nor shovels nor picks. This prevented them from transporting to the fields as fertilizer manure from cattle that were kept close to dwellings at night for security reasons. As a result there had been a massive decline in land fertility throughout the area. One solution might have been to buy huge amounts of fertilizer at a heavy cost in foreign exchange, but this would have made the problem worse because only those farmers with cash incomes could have afforded to buy fertilizer. It would have been simpler and cheaper to set up a domestic wheelbarrow industry.

From this example Dr. Brett drew the conclusion that prices were indeed an important determinant of agricultural productivity since, obviously, "peasants who do not get paid very much for what they produce cannot use what they get to buy the things that they would need to produce more next time." But he added that higher prices paid to producers were not the whole solution. The problem of constrained administrative delivery systems to which he had alluded earlier also had to be addressed. He decribed the problem in graphic terms, noting that there were few shops in rural areas in Africa and that peasants often had to walk long distances through snake-infested paths to reach merchant outlets. He added, "How you actually get wheelbarrows, tools, and so on to those farmers at the end of a filthy track which is often, in winter, in the wet season, thick with mud, [in a country] where the foreign exchange problem has meant that nobody has been able to buy a bicycle for twenty years, is a critical administrative problem."

Dr. Brett agreed with a point made earlier that, where a potentially flexible and dynamic structure of small-scale indigenous entrepreneurship existed, the creation of an intermediate merchant class could not be expected to occur spontaneously. In such a case it would indeed be necessary to work through governments to create appropriate structures. He reiterated that in this context the merits of cooperatives should not be overlooked.

A speaker cautioned against getting "hoist with a populist petard for the NGO sector." He had learned from bitter experience that NGOs were good at delivering health care and education and at mobilization of various kinds but were not very successful in putting efficiently managed productive assets into the hands of the poor. This comment was endorsed by another speaker, who said that there was at present no real alternative to utilizing governments and government entities to reach and have an impact on the poor in the productive sectors or economies. NGOs did have a major role to play in such sectors as health, population planning, and education.

Dr. Brett also agreed that NGOs were more effective in the services sector and added that they were more an Asian than an African phenomenon. He reiterated that the cooperative sector was a crucial one. In arguing for greater flexibility, creativity, and inventiveness with regard to cooperatives, he observed that cooperatives, as they currently existed in some parts of Africa, were not adapted to local circumstances. They had been founded initially on Rochdale principles, and their structures had been based on a set of assumptions about monopoly which the British working class had had to use as a mechansim for developing themselves in the context of a developed retail trade sector. When translated into the African context, however, the structure had become yet another method of stealing resources from the poor.

Dr. Brett complained that economists totally dominated the whole structure of policy analysis; "the last great unexamined imperialist monopoly in late capitalism is the monopoly on economic science." Any serious effort to bring about institutional reform would have to be based on analyses of cases in which such reforms took place in governments and through governments. Professionals would have to be brought in to carry out the analyses; economists should not presume that they were themselves competent to deal with those issues.

The degree of the Bank's continuing commitment to poverty alleviation was discussed again. A speaker welcomed the assurances from the Bank that it was still concerned about the distribution of the benefits of growth and had not turned its back on the McNamara thrust of the 1970s, but he expressed uneasiness that participants in the symposium would get the impression that nothing had happened to the Bank's practices since the McNamara years. He questioned whether the Bank's operational staff were under the same sort of pressure today as they had been five years ago to emphasize poverty alleviation objectives in program designs and project appraisals. The speaker suspected that an honest response would acknowledge that the signals to those making investment decisions affecting poverty alleviation had indeed changed and that there were valid, "nonsinister" reasons for this shift. The most obvious one, in his view, was that the political composition of the Bank's Board had changed substantially and that the group which dominated the Board at present was not in the least interested in poverty alleviation as an objective of Bank policy. He was not in any way impugning the motives of Bank staff and management in suggesting that they could not fail to respond to the dominant voice of those governments that ultimately decided the Bank's policies and provided its access to capital.

Commenting on that statement, Dr. Brett agreed that one had to recognize that the Bank itself operated within a context and framework in which the Western industrial countries had a dominating position both structurally and in terms of their de facto capacity to exercise influence since, after all, they were putting up the money. He pointed out that irrationality was not the exclusive province of the developing world but was evident also in advanced industrial countries that produced and reelected governments which adopted policies that led to some very irrational decisions being made in places like the Board of the World Bank. He expressed sympathy for those Bank staff who were still trying to adhere, in the current atmosphere, to their commitment to poverty alleviation.

The World Bank of Tomorrow: Policies and Operations

D. Joseph Wood

Vice President, Financial Policy Planning and Budgeting, The World Bank

SYNOPSIS. Four points are covered in the presentation. The first relates to the Bank's role in the adjustment process. A summary table giving the main categories of Bank lending in three fiscal years shows that the lending mix has already changed substantially in light of the growing importance of sector loans and nonproject, or program, loans. For the future, no major change in this overall mix of lending instruments is expected, although the mix of recipient countries is likely to be different as the transition is made from the critical phase of stabilization to the phase of resumption of investments.

The second point concerns the status of the Bank's traditional role of supporting specific investments and poverty alleviation operations. The reduction to 40 percent of Bank lending for specific investments is attributable to several factors, including greater emphasis on rehabilitation and maintenance operations, more reliance on sector loans, greater selectivity in support for public sector investments, greater stress on improving management capacity, and assistance in developing sustainable rules of the game for the private sector, both domestic and foreign. As for the emphasis in Bank lending on poverty alleviation objectives, it is true that the signals have changed, but in a positive way. The Bank now wants not only to increase the productivity of the poor directly but also to promote development of a policy and institutional environment that will support poverty alleviation efforts. To this end, the Bank will double its lending for population programs, rapidly expand its support for agricultural research, continue its urban development efforts, integrate themes of cost recovery, deregulation, selectivity in subsidies, and the like, and maintain its emphasis on pricing reforms.

The third point is the catalytic role of the Bank in mobilizing the flow of capital

from other sources. More disciplined coordination of aid is needed. Increases in private capital flows will depend on improved economic management that will restore confidence to commercial bankers and investors. The Bank is actively helping countries to improve their economic performance. In addition, it is working on developing a consensus to create the Multilateral Investment Guarantee Authority (MIGA), and it intends to continue using B-loans as a cofinancing instrument.

Fourth, needs for resources will be a function of the scale of operations which the member governments endorse. Management firmly believes that the Bank has to grow in the medium term so that it can play an effective role in the adjustment process, continue to support investments and poverty alleviation objectives, and be a meaningful partner in the catalytic operations. In the case of IDA funds, a demonstration of the effectiveness of aid will be the key to increasing the volume of official aid, which is expected to be severely constrained in the near term. As for IBRD funds, the Bank is looking to its shareholders to approve a captial increase so that it will have the capacity to sustain lending operations at a considerably higher level than is possible with the current capital base. The consequences of a failure to obtain the requisite amount of capital are described.

One of my responsibilities at the World Bank has been to act as coordinator for an internal exercise to which we have given the title "The Future Role of the Bank." As the coordinator of that exercise, I am reminded of the comment that was made about Winston Churchill—I am not sure when it was but probably in the late 1920s or the 1930s—that he was a young man with a brilliant future behind him! I am in the situation that I now have one and a half futures behind me, having been closely involved in a "future role of the Bank" exercise in the mid-1970s and now being midway through a "future role of the Bank" exercise in the mid-1980s. In that position I have naturally encountered, with all too disturbing frequency, the question, "How is the future of the Bank?" My stock response is "under careful review." That is a safe reply.

I find that people actually are quite frustrated with ambiguities, and I am sure at this time on a Friday afternoon you too must be anxious to be spared the diplomatic niceties and (something which the Bank resorts to with great frequency) the long words which obscure the meaning of what is really going on. I cannot promise you that I will avoid long, obscure words, but I will try to concentrate what I have to say on a few questions which I think are practical and to which the answers, at least in part, can be fairly precise.

I want to touch on four questions. The first has to do with the Bank's role in the adjustment process. The question there is, has the Bank gone far enough in adapting its operations to the evolving needs of the developing countries? In particular, is the mix between what is traditionally called project and nonproject lending right yet?

Second, what about the Bank's more traditional functions of lending to support investment projects and operations directed toward poverty alleviation? This question was raised with particular force at the end of the morning session. I think the chairman paraphrased it as follows: "Will the real World Bank please stand up?" I will try to respond to that question.

Third, something which we emphasize a lot in the World Bank and which has only been touched on here: the Bank's catalytic role—that is, what it can do to encourage others. I will briefly touch on a couple of developments that bear on that role.

Finally, I should mention that I am from the side of the Bank concerned with acquiring the resources rather than with lending them once acquired. Therefore I think you will not find it surprising that one of the questions which I think is relevant in discussing the future is where the money is to come from. What sorts of resources are needed to implement the roles which we have been discussing for the Bank?

First, then, the question of the Bank's role in the adjustment process. The governor of the Bank of England gave a thoughtful speech on the subject of the future roles of the IMF and the World Bank in early December 1984. I think he put the question rather well. He said, "Having discovered that it cannot stand aloof from the adjustment process, the Bank has to determine how far it should change the direction of its lending towards the encouragement of adjustment."

The first question I want to address is exactly that. To make it somewhat specific, I have asked to have passed out a piece of paper (table 4) which gives some factual information on the mix of the Bank's operations. I will not burden you with a lot of definitions. I think most of these titles will at least suggest to you the nature of the underlying operation.

What I want to bring out by citing this historical information is the extent to which the mix of Bank operations has already changed. There are various ways of capturing that change. I think it comes out most clearly in the bottom part of this table, in the percentage shares for the Bank's support for specific investments—that is, where the Bank itself appraises the technical, financial, and managerial aspects of the investment. That type of operation has declined in relative terms from about 60 percent to about 40 percent of our operations.

To go to the other side, the part of our operations which is traditionally identified as being nonproject is the structural adjustment and program loans.

Table 4. *Summary of IBRD and IDA Commitments, Fiscal Years 1980, 1981, and 1984*

Item	*1980*	*1981*	*1984*
Amount (millons of dollars)			
Specific investments	6,941	6,064	6,414
Sector operations			
Sector investments	1,941	2,533	4,113
Financial intermediaries	1,765	2,314	2,043
Sector adjustment	90	244	1,318
Structural adjustment and program loans	355	782	1,272
Technical assistance	125	279	324
Emergency reconstruction	265	75	40
Total	11,482	12,291	15,524
Percentage shares			
Specific investments	60.5	49.3	41.3
Sector operations			
Sector investments	16.9	20.6	26.5
Financial intermediaries	15.4	18.8	13.2
Sector adjustment	0.7	2.0	8.5
Structural adjustment and program loans	3.1	6.4	8.2
Technical assistance	1.1	2.3	2.1
Emergency reconstruction	2.3	0.6	0.3
Total	100.0	100.0	100.0

Note: Items may not add to total because of rounding.

You will frequently hear people say that less than 10 percent of World Bank operations are in program loan or nonproject loan operations. The rest is in what is sometimes called a grey area in between, that is, sector operations. The sector operations are divided into three categories here: sector investment operations, where we are not ourselves appraising the individual investments but are agreeing with an institution or an agency in the borrowing country on the criteria to be followed; financial intermediaries—and that is familiar—where we lend through domestic institutions; and sector adjustment loans, those operations where we agree with the government concerned on policy and institutional changes in a particular sector and the loan is in support of those changes. They represent an application on a sector basis of the same kind of techniques which, applied economywide, constitute our structural adjustment lending.

As you will see, the sector adjustment loans and the structural adjustment loans have risen from about 4 percent of our operations in 1980 to a little more than 16 percent in the most recent years. That is an important part of the Bank's response to the changing requirements of our borrowing governments.

In the discussions we have had internally and with our Board, the broad conclusion about the future direction of the Bank is that these proportions are unlikely to shift dramatically in the future from where they were in fiscal 1984. That does not mean to say they will not change at all, but we do not expect further dramatic changes.

These aggregate statistics disguise some important shifts in composition. The 16 percent of what is sometimes called policy-based operations is not evenly distributed among countries. It amounts to about 6 percent of our operations in South Asia, where stabilization issues are not critical, and 26 percent of our operations in Latin America. In some of the African countries it amounts to an even higher proportion of the total.

Looking to the future, the reason we do not expect that 16 percent to change dramatically is because of a shift in composition. The critical adjustment, the crisis phase, for some of the larger borrowing countries will gradually give way (as it has in Turkey, for example) to a follow-on phase in which the Bank supports sectoral investment operations rather than making structural adjustment loans or sector adjustment loans.

As we phase out of structural adjustment loans and sector adjustment loans in some countries, we expect to see that made up by increased operations of those kinds in the African countries and in some of the smaller middle-income countries where stabilization issues have not yet been successfully dealt with. Hence, in terms of the overall mix of our operations, we think the shift toward adjustment-related lending, in percentage terms, has largely happened already, and although the mix of countries to which these instruments will apply is going to change in the future, we do not expect major differences in the overall composition of lending instruments.

The second question is, what about the Bank's traditional roles of support for investment and for operations directed toward poverty alleviation? As you will see from the statistics, the percentage of lending directed toward specific investments has declined, and rather sharply, from 60 percent to about 40 percent.

The reasons behind that are interesting, and they help in understanding the expected future trends in operations. One of the reasons for the drop in that percentage is that the Bank has already shifted more attention toward rehabilitation and maintenance operations. This is particularly evident in Sub-Saharan Africa, where it clearly made no sense to continue to add to productive capacity when the existing capacity could not be utilized and was not being maintained. Rehabilitation and maintenance will remain a prominent feature of our investment-related operations in the years ahead.

Second, you will see, as I have already mentioned under the sector operations, increased reliance on these particular tools. That reflects the growing strength of institutions in some of our borrowing member countries. We think the shift toward relying on domestic institutions, toward appraising the appraisers, if you like, is a healthy and warranted shift which should be expected to continue. In fact, it has already gone quite a long way in our operations in South and East Asia.

The third point I would make about our support for investment—and this echoes some of the comments which were made in earlier sessions—is that to the extent we are supporting public sector investments, we are acutely conscious of an environment of much greater resource scarcity. That is true in Sub-Saharan African countries and in poor countries generally because of shortages of official assistance, and it is also true in middle-income countries which have traditionally relied on capital markets and where the growth rates of exposure of commercial banks that occurred in the 1970s are generally accepted not to be in prospect for the remainder of the 1980s. Because of that resource scarcity, we recognize that our support for public sector investments has to be much more selective. We have to be much more concerned with the efficiency and the use of the capacity once created, and we have to be more sensitive to the ability of the country to finance those investments out of its own resources.

In trying to deal with those questions, we think that the sector investment loan operations will play a prominent role because sector loans enable us to address the institution-building issues which are important to all those aspects I mentioned.

Selectivity of investment requires in many cases strengthening of institutional capacity to make those project selections. The efficiency in use of the capacity once created is a function of the policy environment, and as was mentioned before, one of the things we are acutely conscious of is that a supportive policy environment is not something that is decreed at one time and then simply continues on automatic pilot. The kinds of policy reform that the Bank is concerned with in the trade policy and credit allocation areas are things which require institutions to continue to implement, monitor, and adjust. When we use the words "anchoring policy reform," we mean trying to support development of institutions which will give the economies the continuing capacity to adapt and to adjust.

On the issue of financing projects out of domestic resources to a greater extent, a good deal has already been mentioned about the public sector enterprises, the parastatal operations, in these countries. It is absolutely critical that the large deficits that these institutions run be addressed successfully. Again, that is not simply a matter of decree; it is a matter of improved management. So, that too will be a focus of our operations in this area.

Now, on the investment side, a word about support for the private sector. We do not believe that adequate growth is going to be achieved, particularly in the middle-income countries, unless these countries are able to capture the dynamisms of their own domestic private sectors and in many cases to draw on the advantages that come along with foreign private investment.

Our concern here is to assist countries to develop incentive systems or, more generally, "rules of the game" which are their rules, which they understand, which are not imposed, but which they develop with help and which they can sustain. The absolutely critical factor for a successful long-term contribution by the private sector is a set of rules which are understood, which are accepted, and which therefore are sustainable, not rules that are adopted under the pressure of the moment and are changed at the first sign of relief.

The Bank has already addressed these questions of the rules of the game in connection with the energy sector. In the aftermath of the two oil shocks of the 1970s it was recognized that there was going to be a need for substantial investment in the energy sector. It was also recognized in many cases that the private sector, both domestic and foreign, had a role to play in this area and that there was a need to get sustainable, understandable rules of the game. The Bank mounted a very extensive program to help countries review and revise the rules applicable to energy exploration and development. This is an action which we hope to emulate and extend beyond the energy sector into the manufacturing and other sectors.

What about poverty alleviation? The question was raised this morning, have the signals changed? Is the Bank today as committed to poverty alleviation in practice as would like to suggest in our speeches?

I think the fair answer to that is that the signals have changed, not because of a lesser commitment to poverty alleviation but because of a recognition that the focus in the 1970s—which was indeed, as one of the speakers this morning correctly mentioned, on increasing the productivity of the poor through investment projects oriented toward and including widespread participation by the poor—is vital but is not enough by itself. It is essential, in support of poverty alleviation, also to have an institutional and policy environment that is supportive of these investments. When I say "policy and institutional environment," it does not just mean adjusting prices to international levels. There are other forms of policy and institutional arrangements which deserve equal emphasis.

In terms of investment, the one decision which has already been made about the future composition of our operations is that our lending for population programs will double. A second conclusion is that the Bank's support for agricultural research will expand rapidly. Both are forms of investment which we think are, in the long run, vital to dealing successfully with, for example, the food balance issue. It is not just a matter, however, of investment, but of services and our work in urban areas. Sometimes when we talk about support for urban development it may sound somewhat utopian in the context of the financial crises which countries are facing. But in fact, looking at specific operations, many of the measures which are advocated and supported through urban projects are very close to the hearts of hard-pressed finance ministers in those countries. The themes of cost recovery, of deregulation, of selectivity in subsidies are all part and parcel of the attempt to have more targeted, more efficient, more effectively managed services. These, although they are relevant to the stabilization issues, are also vital in protecting and enhancing the services that are available to the poor.

Finally, of course, there are the questions of policy reforms which relate to pricing. Here I will just repeat the themes which Shahid Husain mentioned before.

Although there is not a precise correspondence between the policy reforms that would benefit the poor and the policy reforms which are required for stabilization, neither is there complete conflict, and many of the reforms in the pricing area, particularly in agricultural pricing, do benefit the rural poor—not the landless rural poor, I would agree, but at least the rational peasant. Similarly, in the manufacturing area trade policy rationalization can often work to offset biases against labor-intensive manufacturing.

So, the sense we have is that the focus on investment, including the focus on poverty alleviation, must and will remain the mainstay of our operation.

Although somewhat less than 20 percent of our operations will be particularly focused on the stabilization and adjustment issues, the great bulk of our operations will focus on investment and, in ways I have mentioned—via targeted investment services and policy reform—on the alleviation of poverty.

My third question had to do with the Bank's catalytic role. I want to be brief on this; Stanley Please will talk about our program in Africa. To the extent that the Bank interacts with other official agencies and tries to encourage other official agencies, I think the main themes for the future are that aid coordination, which has been around for years, needs to be applied with a new vigor and discipline in the future; that it needs to be country-specific. I think Stanley says the "monkey has to be put on the back" of the government in the borrowing country. I prefer the phrase, "the country needs itself to be committed and in a leadership role." Given country involvement in a meaningful way, it is important that the process of aid coordination be more disciplined than it has been in the past. I will leave it to Stanley to elaborate on that form of the Bank's catalytic role.

Vis-à-vis private capital, let me just mention briefly one fundamental and then two instrumental developments. The first, basic point is that, as far as private flows are concerned, there is no substitute for getting the fundamentals right. Unless the economic management in the country is such as to assure those private sources, whether they are banks or private investors, that there is going to be the basis for either servicing their debt, if it is a bank loan, or realizing profits, if it is a direct investment, and they have confidence that the conditions will be sustained, the mechanisms for providing insurance or guarantees or lending in partnership are palliatives which will really not affect the volume of flows in a major way.

So the primary focus of our catalytic role is, in fact, what we are trying to do in our direct operations, which is to improve the economic managements in these countries. There can be lags in recognizing that improvements have been made. There can be uncertainties arising from past difficulties. In those circumstances where there are lags in recognition or continued uncertainties, we feel there is some scope for action to provide private actors, the banks or direct investors, with that extra increment of security which is necessary to put the deal together.

In respect to private direct investment, we have over the last eighteen months or more been working to develop a consensus in favor of a Multilateral Investment Guarantee Authority, and we are cautiously optimistic that we will be able by the time of the annual meeting in 1985 to have a draft convention, or indeed to be even further along toward the establishment of such an authority.

With respect to commercial bank loans, you are aware of the so-called B-loan techniques. We think, given the difficult environment, the record established with these new techniques is a commendable one. We intend to continue with these instruments and perhaps to develop further the guarantee power of the Bank.

Finally, let me say something about the price tag. What is this going to cost? Is it realistic?

The question of cost depends on the scale of operations. There the shareholders have not yet pronounced, but management has taken a firm position that, to implement effectively the Bank's role in the adjustment process, its support for investment and poverty alleviation, its role as a meaningful partner in connection with the catalytic operations, the Bank must expect to grow in the medium term. How much it should grow is, in the end, a political decision for our member governments to make.

With respect to official aid, which in our case involves IDA, we believe that in the near term there will be severe constraints on the overall growth of official flows and that the fundamental way of dealing with the constraints is to address the underlying concerns about the effectiveness of official aid. That gets back to some of the things I said about aid coordination. If we can establish the effectiveness of aid, we can somewhat relax the resource constraint. The two, effectiveness and increased volume, go together.

So far as the IBRD funds are concerned, I think there is a general acceptance that it is desirable for the future not simply to go back to where we were in the 1970s but to have a better balance between official and private flows, between long-term and short-term finance, and between fixed rate funding and variable rate funding. All of those balance issues would tend to support a growth rate for the IBRD which is somewhat higher than the growth expected in the commercial banking area, where I think most people expect a growth rate of something under 10 percent, much below the rates in the 1970s. Indeed, our own internal preliminary planning assumptions involve a future growth rate of IBRD operations of approximately 10 percent a year, which, if approved—and shareholders have not approved it yet—would permit the Bank to maintain the current level of net disbursement at about $7 billion a year over the next few years.

If the shareholders do not approve an increase in our capital, the prospect is for these net disbursements to begin to fall off rapidly and, within the next three or four years, for the Bank to get into the position which the commercial banks are in now, of taking more money from the developing world than it is putting into it. Frankly, from the point of view of global flows that makes very little sense. It also makes very little sense in that currently the major channel through which the developing countries tap the long-term fixed rate markets of the world is via the World Bank and the regional banks. Were the Bank to go into a holding pattern and reduce in absolute terms its recourse to those markets, it would represent a decision by the international community at this time and in these circumstances to reduce the recourse of the middle-income developing countries to the bond markets of the world.

Finally, with respect to the question of the growth of the Bank, there is the country perspective. We have increasingly over the years emphasized that we are not in the business of financing individual operations but rather of supporting country development programs. In offering such support, what distinguishes the Bank is its medium- and long-term perspectives. It needs to be able, in dialogue with governments, to be a reliable medium-term partner. It cannot be in the business of saying, "Well, we want you to start down this path which may take years successfully to implement, but, frankly, we cannot tell you whether we will have the money to support you beyond this current year." Again, to implement the kind of country relation which we think is essential from the adjustment, investment, and poverty alleviation perspectives, we need to have medium-term assurance about funding availability.

What is required of governments in the case of the IBRD is a capital increase. Most of you know that the capital increase from governments is overwhelmingly in the form of guarantee capital. The last time we had a capital increase, the proportion that was actually payable in cash was 7.5 percent. That represents a de facto ceiling on the proportion of any increase which would have to come from government budgets. As for the remainder, the resources come not from government but from borrowings on market terms, and to implement the kind of growth in lending which I have described, the Bank in fact would not need to expand radically its recourse to capital markets. Its level of net borrowing already has reached the level which, if modestly increased, would support that scale of operation.

To sum up, the bank's role in the adjustment process should be more or less, in terms of quantitative magnitude, a continuation of the position which we have reached today. Support for investment and poverty alleviation will remain the mainstay of our operations. We expect to continue to work on our catalytic role. With respect to official agencies, we will emphasize the primary role of the recipient government, supported by greater discipline in aid coordination. In connection with private capital, we will emphasize getting the fundamentals right and then, when they are right, providing an extra nudge of support through cofinancing and other techniques.

Discussion

As the penultimate speaker and the last Bank official to address the symposium, Mr. Wood found himself in the position, as one speaker put it, "of being an 'Aunt Sally' for us to throw rotten tomatoes at." The same speaker launched into a vivid description of the rather negative image "that most of us have of the Bank." According to her, that image was of an institution that produced well-written, glossy, nice-looking reports, the contents of which were sometimes questionable, and that employed staff who were essentially ignorant of, if not downright insensitive to, the conditions in the countries they were supposed to be helping. The Bank's "man in the field"—and she stressed "man"—was seen as "a jet-setting, highly paid, white male official flying in to spend a few weeks in an area, going around in nice big cars accompanied by local officials with whom he occasionally made short sallies into rural areas (in the dry season, of course), never staying long enough to—nor even wishing to—learn the local language so that he could speak directly with the people he is supposedly working with, particularly the women, who are less likely than the men to speak the colonial language."

This speaker observed that Dr. Brett's presentation had been so enthusiastically received because he had talked about individual people—men, women, and children—who were actually suffering from the effects of underdevelopment and whose needs were for basic things like wheelbarrows rather than for massive financial credits. She also objected to the definition of development which she had understood the Bank to have given during the discussion on default, namely that of "promises by which Third World countries are brought into the international financial system."

Mr. Wood answered that it was indeed the human dimension of development—the "people focus"—to which the public responded, and that the Bank staff's sensitivity to that human dimension was at the root of their motivation. The fact that their professional responsibilities sometimes required them to write reports on seemingly abstract concepts was not a contradiction. It was perhaps possible to criticize the Bank for having inadequate knowledge of local conditions; indeed, an important part of the Bank's initiative in Africa involved strengthening its field office representation to help develop a knowledge base about local circumstances. Such criticism, however, had to be considered in light of the Bank's pragmatism and its willingness to identify and learn from its own mistakes in its lending operations.

Another speaker said that the Bank's definition of development had been uncharitably characterized. In fact, what had been said in this regard during the default discussion was that developing countries needed to enter into a partnership with industrial countries that would put them on more equal terms in international financing and trade relations. At present, major debtor developing countries were severely constrained by having all the obligations of membership in the international trade and payments system without any of the privileges.

Another point made by the first speaker related to the Bank's views on the population issue. Her reading of the *World Development Report 1984*, which dealt with population, led her to conclude that the report's authors thought that tackling the population problem would solve all development problems.

She objected to the report's "racist approach" to population control which, according to her, was based on implicit assumptions about the irresponsibility of people, particularly in Africa, who were unwilling "to control themselves." This view, she said, did not square with the widely known fact that population control was linked with economic welfare, as had been demonstrated in postwar Europe and elsewhere.

Mr. Wood noted that the substance of the report (whose author was a woman) was quite different from the speaker's characterization of it. The report had dealt at length with the relative merits of relying on economic growth and development to solve the population issue or of reinforcing incentives to control birth rates in addition to stimulating growth and development in a general way.

A different speaker inquired what type of expenditure on population control the Bank would support, given that many different initiatives had already been tried by governments without success. The reply was that the Bank was "totally eclectic" on the subject: it would support whatever worked in a particular case. It was willing to work with full-fledged programs such as those that were flourishing in Indonesia and India or to devise programs as components of national health schemes or maternal and child health plans in the hope that these would eventually lead to a broader scope of population activities. The Bank recognized that NGOs had an important role to play in this field and was prepared to collaborate with them where appropriate. It was stated that the Bank's population programs to date had been mostly in Asia, in part because many African governments had until recently espoused pronatalist views. This was beginning to change, however.

Another lively exchange took place with respect to the impact on the environment of large-scale development projects. Deploring what she termed "the appalling environmental deterioration in many parts of the South," a speaker asked whether the Bank was planning either to adhere to the environmental impact policy it carried on its books but allegedly ignored or to examine the environmental cost of some of the projects it had supported. She noted that, at a conference of NGOs recently held in Nairobi to explore the links between environment and development, the Bank had been singled out for the negative impact it was having on the environment because of its support for large development projects and for cash cropping, chemical-based agricultural development, and industrialization.

The Bank was the only major international financial institution that had a specific policy on the environment, it was stated in reply. That policy, which had been adopted as far back as the late 1960s, entailed making specific assessments of the environmental impact of projects being considered for

Bank financing and collaborating with borrowing governments to reduce or eliminate adverse environmental impacts. But, it was pointed out, there was a bigger issue: economic progress in developing countries could not occur without having some impact on the environment. Pressures from population growth and from the need to grow food and to create jobs could not be ignored. Thus, the environmental issue had to be considered as part of the broader concern with overall resource management—a difficult task.

The case of the traditional African agricultural practice of shifting cultivation was given as an example of the type of problem that arose in this context. In principle, shifting cultivation was inappropriate, but in the particular case of Africa it appeared to have worked properly for a long time. People cleared a piece of forestland, cultivated it for some years, and then moved on; the land then lay fallow for twenty or thirty years and could regenerate its fertility. But under the pressure of population growth this practice was in the process of changing. In such a situation, should governments be advised of the inappropriateness of shifting cultivation and be urged to replace it with other agricultural methods? Or should they, in light of the well-entrenched nature of the practice, be helped to determine what could make this form of agriculture sustainable in terms of soil fertility and environmental conditions, and in the face of population growth rates of 3 to 4 percent? It was noted in this connection that the Bank supported numerous agricultural research stations around the world, four of them in Africa, whose work involved problems of soil and water management in fragile ecosystems.

A second example of the Bank's concern for the environment related to its support for resettlement schemes. Where the projects involved clearing forests, the Bank advocated not touching primary forests. Moreover, it encouraged the borrowing governments to consider cultivating crops that would enhance proper soil management. In general, the Bank tried to persuade its borrowers to take seriously the matter of proper resource management, since it was part and parcel of meaningful economic development and growth.

The speaker, partly satisfied with this response, reiterated her concern about the increased acreage being allocated to cash crops for export and the effect this was having on pushing landless people into marginal lands. In her view it was essential to consider the whole set of costs associated with each of the changes being fostered by economic development projects.

By way of reply, she was asked what could be done about the pressure being exerted on the land in Kenya, for example, by a population growth rate of 4 percent a year. There was simply no way to stop people from cultivating those lands.

The speaker objected to this answer on the grounds that it misunderstood the question she had posed. Kenya was a particularly good example of a country where much of the best land was being used to produce export crops. If the blame was going to be put on people who had been marginalized by the destruction of their environment for the sake of export earnings, it was only fair to consider development projects in a wider way and to analyze the factors that affected population growth and change. She deplored the fact that *World Development Report 1984* had devoted some seven or eight chapters to population issues but only a column and a half to environmental deterioration. This showed an imbalance, she said.

In response, it was stated that the issue was not whether export crops or food crops were being grown. This was secondary to the real issue of raising the productivity of the poor and of the small farmer, thereby raising their hopes, opportunities, and incomes. Increased productivity would require more energy in the soil. The concern of the environmentalist and resource manager was to choose fertilizers and pesticides that would not have a lasting adverse impact on the environment. The Bank was working with other agencies to devise guidelines on which fertilizers and pesticides were appropriate for financing.

The speaker responded that the crux of the problem was not to ameliorate the effects of the chemical input to cash crop agriculture but to identify what type of agriculture would sustain human needs over the long term and to find ways for the Bank to support that type of agriculture in developing countries.

The final point made in this part of the discussion was that devising ways to fix nitrogen in the soil without the use of chemicals was the key challenge currently confronting agricultural researchers, biologists, and breeders. The trend in agricultural research in the past three or four decades had been toward high-energy agriculture. Indeed, the green revolution had been brought about through application of more water, more fertilizer, and more pesticides.

The Bank's catalytic role with respect to aid coordination was brought up by two speakers. One praised the Bank's efforts to coordinate the aid flows through various consultative groups and consortia it had helped establish for many individual borrowers. But he saw less evidence that the Bank was doing much to coordinate its activities with those of other U.N. agencies such as the World Food Programme. The other speaker said that, notwithstanding years of talk about the need for it, there was still a long way to go before an effective aid coordination operation was in place. One aspect of effective coordination surely was effective consultation, he said, and he sharply criticized the Bank for its "horrible reputation" in this regard. In his experience, the Bank had a habit of being less than frank in its dealings with others involved in financing a given project. The speaker urged the Bank representatives at the symposium to tell their colleagues working in operations to be much more open with other donors about what the Bank was thinking, doing, and saying to its borrowers. While he realized the Bank would probably not find it easy to accept the notion, "it was not absolutely out of the question that other donors—even bilateral ones—might have some useful advice to offer even the Bank." If the consultative aspect could be improved, there was a good basis for cooperation in a number of fields. The United Kingdom had taken some initiatives in the United Nations on population issues and was interested in "doing something on crop forecasting." The speaker reiterated his hope that the Bank would "take its responsibilities and act as a leader to the bilateral donors and other multilateral donors in the appropriate fields." Indeed, he considered it crucial that the Bank do this if it meant to be a catalyst for resource flows to developing countries.

The first of these two speakers followed up with a question about how the Bank and the regional development banks sorted out their proper respective roles. Mr. Wood replied that the balance between the global and the regional institutions was achieved in much the same way as it was achieved between multilateral and bilateral aid, the respective strengths and weaknesses of each being complementary to one another. The amounts of money channeled through the regional banks varied. The Inter-American Development Bank and the World Bank were roughly comparable in scale; the Asian Development Bank was smaller than the World Bank but was growing rapidly. The hard loan resources of both regional banks had recently been expanded in a multiyear replenishment exercise that would permit their commitments to grow by 12 to 15 percent a year for several years. Their soft loan resources would be coming up for replenishment in the near future.

A speaker took note of the Bank's growing involvement in the politically charged area of structural adjustment and of the consequent need for it to demonstrate success in this nontraditional type of lending if it hoped to obtain the support of major shareholders in the future. To achieve this end, the speaker said, it was necessary for the Bank "no longer [to] be run by management." It was time that the Bank's Executive Directors played a greater role in the Bank's operations, giving management and staff alike "more power to their elbows," as was the case in the IMF, he said. A structural change in the Bank itself with the goal of restoring some power to the Executive Directors would not only help the staff in their dealings with borrowing countries but would also strengthen the case for a general capital increase. Prompted by these remarks, the chairman recalled that a question about how a Bank project officer out in the field was affected by the change in climate or policy direction within the Board had not yet been answered.

Mr. Wood replied that the comments substantially exaggerated the influence of these political crosscurrents on the person in the field trying to put together an operation. That individual was more likely to be responding to the immediate macro and micro preoccupations of the borrowing country and to the need for setting projects in an appropriate policy environment than to assumptions about what might be popular with the Board.

This response elicited from a different speaker (a former Executive Director) a number of comments on the power and influence (or lack thereof) of the Bank's Executive Directors. He pointed out that the Bank always seemed to ascribe greater power and influence to the Executive Directors than they themselves felt they had. In connection with a subject that had been raised earlier, he attributed the apparent and real diminution of concentration on poverty alleviation programs more to considerable disillusionment with the type of integrated rural development projects that were popular in the mid and late 1970s than to "malevolence on the part of Board members." Many of these projects had encountered various technical problems—inadequate design, weak institutional structures, insufficient power, and so on—that had ultimately caused them to fail to meet their objectives, he said.

A speaker wondered whether the Bank would be weakening its own position in the overall aid picture by shifting its emphasis away from direct project lending, where its efficiency, knowledge, and experience in project design, financing, monitoring, and implementation gave it a comparative advantage over other donors. Moreover, by moving into the highly political areas of adjustment lending, was the Bank not, in addition, weakening the whole position of multilateral aid, which had heretofore been perceived to be further removed from politics than bilateral aid?

Mr. Wood acknowledged that the Bank was moving away from its traditional strengths in project lending, but this was happening in response to evolution within the borrowing countries, many of which had internalized the sort of technical know-how that had been provided by the Bank in the past. The comparative advantage was changing. Were the Bank to stick to its traditional strengths, it would be missing the boat in some countries. This was not the case in many parts of Africa, however, where borrowers would continue to rely on the Bank's capabilities for technical, financial, and managerial appraisal of individual projects. As for the risks of politicization presented by the Bank's growing involvement with adjustment efforts, it was thought that the multilateral character of the Bank would make it easier for it to attempt to address such concerns. In contrast, bilateral agencies trying to do this would find it difficult to avoid giving a political coloration to their efforts.

Another speaker took note of the similarity between the Bank's mix of project and nonproject lending and that of the United Kingdom's Overseas Development Administration. He also pointed out the contradiction between the preceding speaker's view that the Bank had a comparative advantage in project lending and the view expressed in Stanley Please's *The Hobbled Giant* (1984) that the Bank's comparative advantage was in structural adjustment or program lending and that project lending should be left to other donors. His own opinion was that bilateral and multilateral donors alike would increasingly be involved with both kinds of aid because these responded to the current needs of the developing countries.

In reply to a question on graduation from aid, Mr. Wood noted that some countries were currently paying money back to the Bank. One of these was Japan, which had been a major borrower from the Bank several decades ago. The statement that had been made in the presentation about the consequences of the Bank being perceived as taking more money out than it was putting in referred to the political reaction, not to the economic effects. There had been extensive debate within the Bank over the graduation issue, but it had not led to much change. Concerns had been voiced that the graduation process be handled in a collaborative rather than a mechanical fashion. In the Bank's view, this had always characterized its approach.

Finally, a speaker asked whether it would not be appropriate for the Bank to enter into a policy dialogue with donor governments. He urged the Bank to take the risk of "biting the hand that feeds you" for the sake of focusing the developed countries' attention on the policies and actions they had taken which contributed significantly to the negative external environment in which the developing countries now had to function. He cited the high interest rates that currently prevailed, as well as the growth of protectionism and the disruptive effects on global agricultural trade of the European Community's Common Agricultural Policy.

Mr. Wood pointed out that the Bank was not silent on the aspects of the trade regimes of industrial countries that had a bearing on development issues. Its *World Development Report* was one of the vehicles by which the Bank conducted this policy dialogue with the developed world. But the Bank depended on the support of its member governments; although it could and did call attention to the implications of policies for development, it was not in a position to effect political changes in those governments, however much it might desire those changes.

Development Priorities for Sub-Saharan Africa

Stanley Please
Former Senior Adviser to The World Bank

SYNOPSIS. The World Bank's report (1984c) *Toward Sustained Development in Sub-Saharan Africa* [of which Please was principal author] should be seen in the broader context of the Bank's unfolding role in Africa and of the issues that surfaced during the symposium. People are looking to the Bank for leadership on African problems, but there is a deep ambivalence about the Bank. The "reactionary" view holds that the Bank should be tougher in requiring adjustment on economic, political, and social issues in Africa; the "radical" view holds that the Bank is too closely linked with the IMF and cannot be trusted to deal with African problems sympathetically and realistically. The Bank has to acknowledge that these concerns exist and that it is perceived—however inaccurately—as an arrogant institution.

A broad consensus has emerged on the major issues involved in reversing the disaster in Africa. Views have converged on the following points.

- The anti-agricultural bias in Africa has to be reversed, and agricultural development must be based on smallholder development.
- The balance between production of food and of export crops will vary from country to country and from one region to another within the same country; development of intra-African trade in food is more desirable than individual country self-sufficiency in all commodities.
- The import substitution–export orientation controversy has been overblown; a properly balanced policy would not only reduce import intensity, which is unsustainable at present levels, but would also increase exports, where African performance is much below that of other developing countries.
- The privatization issue is a nonissue. Contrary to what was alleged when the Berg report (World Bank 1981) was issued, the Bank does not favor expanding

the role of transnationals; rather, it is urging development of the small-scale end of the private sector, particularly in services, such as marketing and transporting agricultural commodities from farms to local centers.

- Population growth is being increasingly recognized by African leaders as a problem.
- So too is environmental degradation, to which the Bank is calling more attention.

What is needed now is reciprocal conditionality—programs formulated and prepared by individual African governments for specific actions to implement stated objectives and donor programs to sustain and support these African efforts. The Bank's role is to be the catalyst for this reciprocal action, to provide greater discipline to the process of policymaking within Africa, and to monitor donors' adherence to their part of the bargain. To do this effectively, the Bank has to avoid being out on a limb on its own. It has to develop and strengthen the consensus and obtain clear support for its actions from individuals and groups such as those participating in the symposium, as well as other U.N. agencies, university and media people in Africa and elsewhere, and professionals of all kinds in donor countries.

Joe Wood, in response to the comments made about the image of the Bank, said he would make the most humble speech ever. In fact, this is the point behind much of the formulation of my short presentation. What I want to do is not to go through the Bank's report on Sub-Saharan Africa—most of you have read it and many of you have attended lectures I have given on the subject—but to think of that report in the broader context of how the Bank sees its unfolding role in Africa and, specifically, to look at the problem in the context of many of the issues that have been raised at this symposium over the past couple of days.

What I sense at this symposium, and what I sense in going around the country talking on this subject to various groups, is a deep ambivalence toward the World Bank. On the one hand, most institutions and most individuals seem to be looking to the Bank to provide leadership to Africa and to the world community involved in Africa in trying to avoid the reoccurrence of the sort of disaster that these countries are facing. Donors and the general public are asking where we go from simply keeping men, women, and children alive, and what the Bank is doing to avoid similar disasters. I think African governments are looking far more to the Bank. I think the IMF has recognized that, unlike the situation in Brazil, Mexico, the Philippines, and so on, Africa is not its sort of problem. As Nick Hope put it yesterday, if you were to abolish Africa's external debt overnight, you would still be left with fundamental problems of development because you would still not have the solid economic base that you have in most other parts of the developing world. So I think a lot of people are looking to the Bank for leadership. I think that whether the Bank can respond to this challenge will be a real test of the Bank and of its managerial leadership over the next five years or so.

But there is an ambivalence in people's minds as they present this challenge to the Bank. I think the ambivalence arises from two quarters, what, with a danger of oversimplification, one might call the radical group and the more conservative or reactionary group.

On the reactionary side, I think there is the view that the Bank still lingers under the shadow of McNamara; that it is a bleeding-heart organization; that it is in danger of "throwing money at problems"; and particularly, many would say, that it has none of the toughness for addressing those problems that the IMF has. Therefore, in more reactionary circles there is concern, I think, that the Bank is not going to show the toughness that is required on the difficult economic, political, and social issues which have been discussed in this seminar and in many other places and which are critical for reversing the downward trends in Africa.

Second, there is an ambivalence in radical circles that, despite the protestations its managers and staff make to the contrary, the Bank is too linked to the IMF; it is too linked to notions of trickle-down growth; it is too linked to the notion that if you get the prices right, development automatically occurs; that it has moved away from a focus on the poor. In other words, there is ambivalence in radical circles as to how much the Bank can be trusted to deal with the problems in Africa in a sympathetic but realistic sort of way.

It seems to me that the Bank has to recognize all these concerns. It also has to recognize the concern that it is seen as a very arrogant institution. I think this image is understandable in terms of the way the Bank behaves in its operations. I believe, however, that this image is an absurd caricature of the institution, in the sense of the way it wrestles with problems both internally as well as with outside bodies. But I can understand how it has developed this image, and I think that it is an image that it needs to be very concerned about.

I hope this sort of symposium will be useful in trying to dilute that image. Moreover, I think the experience of the past three or four years should give at least some confidence to the doubters that the Bank should be able to deliver on its responsibilities to Africa.

Ted Brett this morning, I hope not just to flatter me, indicated that he found what he called the Please report more acceptable in terms of its analysis and conclusions than the Berg report. I think to the extent that it is true—and the reports are significantly different—it is because the Bank has learned a lot over the past three or four years. I think that this learning has resulted from the broad dialogue that has taken place between the Bank and the various parties that criticized the Berg report, particularly certain people in IDS.

This criticism has been valuable. It has enabled the Bank to sharpen its own position on certain issues. I would like to think that in those discussions the views of others have also been sharpened and perhaps modified. I might even say this to our chairman, the director of the IDS. What I have seen develop over these years—and these were not empty words in the African report—is a growing consensus on what the issues are in Africa. That is an extremely important assertion in the Bank's report. If the assertion is wrong, this error of judgment needs to be emphasized because it is an extremely important assertion that I was anxious to make in the report, and that the Bank was willing to accept.

If it is true that there is a greater consensus, I think that has to be put across very strongly from all quarters. What has tended to happen is that all parties have tended to make discussion out of disagreements. That is all good fun, and it is interesting in the professional literature, but policymakers in Africa and in the donor communities need to be told clearly that in fact there is a broad consensus on the major issues that are involved in reversing the disaster in Africa. The Bank, for its part, has got to continue to develop that consensus with broad groups throughout the world.

One of you asked, very justifiably, what relation the Bank has developed with other U.N. agencies. One U.N. agency with which we have developed a very close agreement is the Economic Commission for Africa (ECA). Three or four years ago the ECA, the African Development Bank (ADB), and the Organization of African Unity (OAU) were staunchly aggressive in their opposition to the Berg report. Now the ECA and the ADB have put out their 1984 economic report, which sounds very much like a modified World Bank and IMF report with all the issues there. That seems to me to be a very important step forward in terms of greater understanding, but it has got to become much broader. As the Bank advances in this responsibility which is being put on its shoulders in Africa, it has got to make sure that it is being backstopped by other organizations, not only by the United Nations but by universities and the media in Africa and by professionals in donor countries, including the United Kingdom. It seems to me there has got to be much more recognition that the Bank is simply reflecting professional views and the views of many other institutions and not arrogantly asserting its own particular recipes for the improvement of policies in Africa.

If one goes through the list of issues that have been raised in the Bank's report and in the discussion in the past two days, one sees major areas of agreement. The whole antiagricultural bias in Africa—the fact that fiscal policies, pricing policies, institutional policies such as in agricultural research, and economic strategy have tended to be antiagriculture—somehow has got to be reversed. I think everyone agrees with that. Moreover, there is almost universal agreement that agricultural development has to be very much on the basis of smallholder development. I say "almost universal" because although technicians in and outside Africa agree, there is a widespread view politically in Africa that Africa needs to take a giant step forward that can best come from large farms, whether they are state farms or in the private sector. There is still, therefore, a problem at the political level in many African countries. Among the technocrats inside and outside Africa there is much more unanimity on this issue. Certainly the ECA, as an intellectual leader in Africa, is emphasizing the importance of smallholder development, both in the areas of high potential and in the areas of low potential.

There is much more agreement on the whole question of the balance between food and export crops than there was three or four years ago. Clearly, that balance is going to be different in different countries. All these issues raise country-specific issues. The Bank was clearly seen, as a result of the Berg report, as pushing overwhelmingly for the development of exports from the agricultural sector, as opposed to food production. Now there is much more of a meeting of minds on that issue. The Bank's position has, in fact, become much closer to the views of its opponents. I think what the Bank was concerned about in the Berg report was the fact that in some countries large volumes of investment resources were going into the production at a very high cost of imperial [high-quality] grains that were frequently subsidized for relatively well-off consumers in those countries. That was and remains a major concern for the Bank, which it emphasized in the Berg report. When I have put this issue to radical groups and said, "Do you believe that African countries should go for self-sufficiency in those sorts of crops for those sorts of people and with those sorts of subsidies?" they have said, "Of course not." I find more and more that as one confronts specific issues with radical groups, the World Bank's position and the position of others become much closer. In Africa the ECA has taken the understandable view that the balance between food and cash crops will vary between regions in different countries and between one country and another. There is certainly no reason why one country should be self-sufficient. It should develop trading relations with another country for its food supply in Africa so that inter-African trade can develop from food at the first stage and then move into industry. Here again, I see much more of a meeting of minds.

I think the whole import substitution–export orientation controversy is a noncontroversy in general, and it certainly is so in relation to Africa. In the

Berg report, however, the export side of the account was perhaps overemphasized, simply because Africa had done so pathetically poorly as against other developing countries in exports of those commodities in which it could be expected that Africa would have a comparative advantage. The development strategies that African countries have embarked on have been completely unsustainable in terms of their import intensity. There has to be a strategy which reduces this import intensity in energy, in food, and in industry. Policy must concentrate both on reducing import intensity and on developing exports.

If instead of using the term private sector in the Berg report we had used the ILO language of the "informal sector," I do not think there would have been any of this hullabaloo. What the Bank is emphasizing is marketing and transport of agricultural commodities from the farm to local centers. Therefore what is being talked about is very much the small-scale end of the private sector, and particularly the service sector. The Bank was interpreted, however, as favoring transnational corporations. Transnationals have a role to play in Africa, but that was not the major focus of the Berg report.

It seems to me that there is much more of a meeting of minds on this question of private sector as against public sector. Probably the peasants, rather than economists, are the best people to choose between these sectors. Let them choose according to which gives them the best service, the most ready payments for their crops, the most efficient supply of inputs. Then, let the system develop on the basis of a joint private sector–public sector involvement in these supporting services.

Turning to another important issue, I think there is now much more agreement on population growth among the African leaders than there was three or four years ago. Clearly those programs have to come from Africa. They cannot be imposed from outside. They have to be consistent with political and social considerations.

The Bank has also given more emphasis in its latest report on Africa to the concerns about environmental degradation that were expressed earlier.

In general, therefore, as I go through the list of supposed disagreements between analysts of the African problem, they seem to fade, if not disappear. What is required now is that national governments address the problems through their own programs. The monkey has to be on their back. Having stated their objectives, national governments have to say how they are going to implement those objectives in terms of changes in policies, institutional arrangements, budgetary policy, and so on. To date, development plans have tended to be empty of operational policy content. They have got to be converted into national operational programs. There is no way in which the Bank can draw up these programs and impose them on a country. It is not like an IMF program for handling a financial emergency. The programs we are talking about have to last for five or ten years, and they have got to be politically acceptable to the government. My own view is that the Bank's role is not leverage; it is the provision of much greater discipline to the process of policymaking. In African countries policymaking is fragmented between different ministries, and the Bank's role is to be a catalyst for action.

This also applies to the donors. The Africa report has come up with what might be called reciprocal conditionality. There must, to begin with, be programs from African governments, but in addition there have got to be donor programs to provide adequate and sustained support to the African programs as they come to be formulated and prepared and implemented.

If the donors are to provide this support, the issues are clear. There has to be less emphasis by donors on grandiose projects and on projects per se and more on rehabilitation and maintenance of existing capacity. There has to be more support for policy reform, which is extremely difficult to do politically and therefore requires a phasing of adjustment, during which much more support is required. This increase in donor assistance is justified during the adjustment period, even though African countries are already the recipients of levels of per capita official development assistance four or five times as high as that going to the Indian subcontinent, where the income per capita is lower than in many African countries.

The case for increased assistance to help countries introduce programs of policy reform has now been accepted by donors. There has been a reasonable response to the Bank's attempt to mobilize funds for its Special Assistance Facility for Sub-Saharan Africa. The purpose of the facility was clearly to establish it outside the normal IDA and IBRD funding and, in doing so, to make it clear, both to donors and to Africa, that the Special Facility would only be activated when programs responsive to the deep needs of an African country were forthcoming; that these special funds would not be programmed into the normal activities of the Bank but would be set aside to help countries implement their programs of adjustment and rehabilitation.

Discipline has therefore to be imposed by the Bank on donors as well as on African countries. The donors have, to begin with, to be committed to ensuring that their project assistance goes only to those projects that are regarded as essential priorities by the African governments in presenting their programs, and second, that the amounts and timing of nonproject assistance support policy reform. If donors do not abide by their undertakings in this regard, the Bank should blow the whistle and make it clear that the donors are not honoring their part of the agreed conditionality.

It seems to me that this is what is required on the donor side if donors are serious when they ask for greater coordination of aid. Greater coordination of aid means greater commitment to using the aid for supporting a program put forward by an African government. If that support is not forthcoming, if projects are selected by a donor for commercial or other reasons, it is for the Bank to make this clear at consultative group meetings, to publicize it, and, one hopes, to bring the offending donor back into the fold of supporting the African government's program.

That really is the point at which I would end, because I believe the Bank's role is not leverage per se; that is a wrong way of expressing the approach that the Bank must adopt if it is to be effective. The approach has to be one of inducing much greater discipline on the part of African governments and of donors, in terms of their respective responsibilities.

In undertaking that process of greater discipline, I think the Bank has got to reach out, particularly through its operational departments, for much more support from the sort of groups represented at this seminar—from the universities, the NGOs and the U.N. agencies, particularly those operating in Africa. The Bank should not be out on a limb on its own. It has to make sure that in helping governments formulate programs it has behind it the profession and NGOs and those concerned about Africa. If it does not have this support, then it should make sure, by eyeball-to-eyeball discussions with representatives of those groups, that the issues are resolved. I think the sort of meeting that is taking place here needs to be magnified if the Bank is going to be able to deliver on the responsibility of providing greater discipline to the process of policymaking and donor support over the next five years or so.

Discussion

A speaker strongly supported the idea that the Bank should play the type of catalytic role described in the presentation. Citing an example in Sudan in which the Bank had succeeded in persuading the government not to neglect the cotton sector, he said it was "essential for the Bank not to be frightened of the political issues involved in these questions." He hoped the Bank would continue to play both its economic and political roles "with self-confidence, not arrogance." He regretted that the United Kingdom had failed to support directly the Bank's Special Facility for Sub-Saharan Africa. He added that it was indeed necessary to get all parties—the Bank, the governments concerned, the NGOs, and the other donors—facing in the right direction simultaneously. This was not happening at present, he said, and he noted that without such coordination things would continue to go wrong and resources would not be put where they should be.

A different speaker concurred with Please that a consensus was emerging on the nature of the major issues facing Africa, but he observed with regret that poverty alleviation was not among them. He drew attention to the fact that the report *Focus on Poverty* (World Bank 1983b), which apparently never achieved much prominence, had suggested that the poverty focus was being lost as structural adjustment lending developed. He felt that the fragile consensus would break down after a few years if there was no evidence of a poverty focus to achieve redistribution with growth within the process of policy reform. Furthermore, he noted, there was a notable exception to the otherwise nonpartisan consensus: the United States.

With respect to *Focus on Poverty*, it was noted that it had led directly to new instructions to Bank staff about the need for a continued focus on alleviation of poverty in Bank lending operations. Moreover, the Bank was henceforth to report yearly to its Board on the poverty focus in its work. These reports would become public after they had been considered by the Executive Directors.

Another speaker asked whether there was in fact as much consensus with respect to aid coordination as was being assumed. Many bodies were using the same terminology on this subject, but she doubted that this amounted to a consensus. The World Bank, the European Development Fund, and the United States, among others, were all talking loudly about coordination, each one assuming that it would be the entity doing the coordinating. The speaker also expressed some concern about the widespread emphasis among donors on program-type lending as opposed to project lending. Addressing whole sectors seemed to be the thing to do. The United States appeared quite keen on this; its pet sector was the free market. She had recently heard a number of senior U.S. policymakers say how they were going to "coordinate" the Bank, Brussels, and even the bilateral Europeans "to think free market." How was the Bank going to reconcile programs and projects and everybody's desire to coordinate and nobody's willingness to be coordinated?

In response, Please said that the Bank was genuinely convinced that the coordinating would have to be done by the governments of the recipient countries themselves, not by outsiders. The outsiders could help make sure that the recipient governments accepted their coordinating roles and were organizationally and administratively equipped to undertake them. The pseudo-colonial notion that the Bank, or the U.S. Agency for International Development, or the Europeans would somehow be in charge of these coordination efforts was doomed to fail in terms of enabling the recipient governments to internalize the whole responsibility. The Bank's latest report on Africa stated unequivocally that only national governments could—or indeed should—undertake the coordinating function, although they would need help in developing the discipline necessary for doing this effectively. He felt strongly that using any other approach would be "the kiss of death" for the aid coordination concept; it had to be done by the recipient governments themselves.

The catastrophic circumstances in which Ethiopia currently found itself were alluded to by another speaker, who made the point that elected public officials in donor countries had a hard time squaring their requests for more funds from their bilateral aid agencies with their electors' perceptions that aid money was being used to buy arms to prosecute civil wars. Such officials would welcome it if international agencies like the Bank would take a more forceful approach to those borrowing countries that wantonly disregarded "the general international consensus of what would be in their best interest." It should be put to such countries that "if you do not do it this way, then you are not going to do it with our money." When many people were suffering and dying, as they were in Ethiopia, there was no time for donors to have scruples about whether such an attitude was paternalistic or neocolonial in nature, this speaker argued.

In response, it was pointed out that there were limitations on what international organizations such as the Bank could do in such situations. If the Bank was going to be expected by donors to take tougher positions toward certain borrowers in the future, it would have to have larger resources supplied by donors as well as consistent support from those donors for its stance. Unfortunately, in the past donors had not always "been with the Bank," commercial interests often having prevailed.

Please commented on the question of how pushy the Bank should be in cases like that of Ethiopia. When Tanzania introduced its Ujaama program in the early 1970s, the Bank asserted unequivocally in public documents that the policy was a nonstarter agronomically because of the likelihood of overgrazing when people were grouped together in areas that had been nomadic. Nevertheless, to avoid appearing excessively assertive or arrogant, the Bank undertook to help the Tanzanians try to make Ujaama effective in terms of agricultural growth, delivery of educational and health services, and so on. The Bank had learned a lot from that experience, not the least of which was that it had to take tougher positions on such issues in the future. It could only do so, however, if it had proper backing from all elements of the international donor community. Without such support, it would be dangerous for the Bank to state bluntly to a borrowing government that it was not willing, for example, to finance projects that involved large-scale estate farms that it knew would fail.

A speaker suggested that the Bank could make a great contribution to the cause of international aid by stressing the need and increasing the capacity to share information about lessons learned from experience by the aid agencies. In his view the Bank and other lenders had learned from their own mistakes but had repeated each other's mistakes to a deplorable extent because of the weak feedback mechanisms within the donor community. Please endorsed this view, adding that he hoped the Bank would become more active in this field.

Concluding Remarks by the Chairman

Mike Faber

If you look at your programs you will see that, modestly concealed between brackets, there is a note to the effect that at this point your chairman will "review the earlier discussions of the symposium." Rather than try to summarize, I shall simply put in order some thoughts that occurred to me while I listened to what was said.

My theme is contrasts, and I shall string my pearls together in the form of a dozen sets of contrasts—contrasts in perceptions of what the World Bank's role and responsibilities have been, are, or ought to be.

The first contrast is implicit in the Bank's own initials—IBRD—and stems from the Bank's early role. The contrast is between the "R" for reconstruction and the "D" for development. The reconstruction was of Europe; development was to be of what were then called undeveloped countries. Europe already possessed the skilled manpower, the institutions, the underlying culture, the political determination, and—with some reservations—the appropriate policies to make a rapid success of reconstruction and rehabilitation. The emphasis thereafter shifted to assistance to developing countries. In such countries the manpower, the institutions, a culture compatible with modernization, and appropriate policies have sometimes been present and have sometimes been found to be missing. Now we face the prospect that in the developing world also much of the work that the World Bank has to do will consist as much of reconstruction and rehabilitation as of new development.

The second contrast is between the Bank as lender (or colender) to governments in support of a whole program of measures and the Bank as lender exclusively for individual projects. Here, too, we are seeing a movement back from project to program lending.

The third contrast is between the Bank as lender for infrastructure projects only, as opposed to lending for the more difficult work of producing tradables—more difficult because success in such cases depends on helping to establish an enterprise whose costs have to be kept below the proceeds received from the sale of its products.

The fourth contrast is between the Bank as a source of finance for the public sector only, as opposed to the Bank as a source of finance—often indirectly and through local finance corporations—for the private sector.

The fifth contrast is between the Bank as provider of finance for physical projects only, as opposed to the Bank as provider of technical assistance. The Bank—so I am told—now finances more technical assistance even than the United Nations Development Programme. That assistance goes for education, training, extension work, and institution-building.

The sixth contrast is between the Bank as promoter of efficient economic policies and sound management, as opposed to the Bank as the apparent supporter of one particular type of political economy. It seems to me that one of the failures of the World Bank has been a failure to make clear, in countries which have embraced some form of "African socialism," a distinction which is vital. That distinction is between an attack on the inefficiency, bureaucracy, and poor management of parastatal organizations (shortcomings which make them a burden not just on the exchequer but also on the shoulders of the peasants) and an attack on the existence of the parastatal organizations themselves and thus on the political philosophy of the governments concerned.

The seventh contrast is between the Bank as a lender and borrower of money, as opposed to the Bank as a development agency. There need not always be a conflict between these two roles, but we deceive ourselves if we pretend there never is. For instance, looking at the foreign debt situation of some smaller countries today, one would say that if they were not countries but companies the proper advice to give them would be that they were insolvent, that they should be put into the hands of a receiver or possibly into liquidation, and that they should settle with their creditors for 5 or 10 cents on the dollar and hope that when economic conditions improved they would be able to start trading again. But however sensible and necessary this advice is, it is not the kind that the World Bank is able to give. There are also occasions when investment agreements need to be renegotiated. The staff of the Bank privately recognize this, but the Bank as a lender of money cannot openly espouse the renegotiation of any such agreements. In respect of conditionality, the advice and technical assistance which the Bank now stands ready to offer may well be such that sounder financial policies will result. That is all to the good. But self-determination and the freedom to make one's own mistakes are part of what development is about. In that sense, the levered imposition of policies dictated from outside is a negative factor in development.

The eighth contrast is between the Bank's mission to alleviate poverty and what is actually happening. A smaller IDA, a greater emphasis on the IFC, increased interest rates on loans, the move to greater cofinancing with the private sector, further emphasis on structural adjustment lending: none of these (except perhaps the last) are poverty-focused measures. Even the insistence (in what we heard from Mr. Raison yesterday) that staff levels within the Bank should be reduced is in this respect perverse. For we all know that lending for poverty alleviation is staff-intensive.

A ninth contrast is between the Bank as adviser and informant and the Bank as enforcer ("we have ways to make you adjust"). Sometimes, indeed, the changes that are enforced are made necessary because the advice which the Bank had earlier given—I am thinking about commodity price projections, for instance—itself has turned out to be wrong.

A tenth contrast is between the Bank as servant of its own ideals and Articles of Agreement, as opposed to the Bank as instrument of the interests and the policy prejudices of its strongest members.

An eleventh contrast is between the Bank aloof and the Bank as part of the United Nations family. It requires almost an effort of will to remember that the Bank was founded as one of the specialized agencies.

So I come to my twelfth contrast. This contrast is between the Bank as a monolithic, omniscient, and sometimes somewhat arrogant institution (and I have borrowed that last adjective from a recent article in *Finance and Development*), as opposed to the staff of the Bank as a collection of concerned, hardworking individuals, modest about what they know, realistic about what they do not know, and, rather like the rest of us, searching for answers to some very intractable problems.

What fascinates in respect of the World Bank is how these contrasts—which are also sources of potential conflict—arise, how they develop, and how they are accommodated and reconciled within the Bank's own structure and policies. My final thought is that it is hugely important that those processes of change should be wisely guided and widely understood. If this symposium has helped toward those ends, the time we have spent here will have been well worthwhile.

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THE WORLD BANK

Headquarters
1818 H Street, N.W.
Washington, D.C. 20433, U.S.A.
Telephone: (202) 477-1234
Telex: WUI 64145 WORLDBANK
RCA 248423 WORLDBK
Cable address:
INTBAFRAD WASHINGTONDC

European Office
66 avenue d'Iéna
75116 Paris, France
Telephone: (1) 4723-54.21
Telex: 842-620628

Tokyo Office
Kokusai Building
1-1, Marunouchi 3-chome
Chiyoda-ku, Tokyo 100, Japan
Telephone: (03) 214-5001
Telex: 781-26838

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