Board Meeting of January 15, 1998
Statement by Jan Piercy

INDIA - Country Assistance Strategy

1. This is a particularly important Country Assistance Strategy. Not only is India one of the largest borrowers from the World Bank Group, but it still faces the daunting challenges of widespread poverty -- with 300 million or 35 percent of the population below the poverty line. While progress in poverty reduction has been steady, it has been uneven and slow. As noted in last year's country study on India (India, Achievements and Challenges in Reducing Poverty), there is a wide range in poverty reduction among states and serious inequalities persist across gender, castes and ethnic groups. The study emphasized that poverty in India is remarkably responsive to economic growth. It also highlighted the important link between investment in human resources and progress in poverty reduction.

2. I therefore welcome the CAS 's central focus on helping to facilitate India’s goal of accelerating growth with equity. We believe the targeted 7-9 percent annual growth is clearly within India’s economic potential, but are skeptical such growth can be achieved and sustained in the absence of more serious efforts at reform. As the CAS notes, the public sector deficit is still far too high, and there is substantial scope for financial sector, trade and regulatory, and public enterprise reform.

3. Recent events in Southeast Asia underscore the importance of strengthening the banking sector, and ensuring transparency, accountability and other aspects of good governance throughout the financial sector. Unfortunately, the Government’s enthusiasm for reform appears largely stalled. While we welcome the fact that some of India’s states are beginning to formulate major economic reforms, India’s prospects for achieving targeted growth would be far more encouraging if the momentum for reform were evident at both the federal and the state levels. Needed trade and investment liberalization, for example, must come from the federal Government.

4. We appreciate the CAS’s unusual degree of candor on program and policy shortcomings including those on both the Indian and Bank sides. This is welcome, although there are also some missed opportunities to speak even more directly about deficiencies, such as the Government’s relative neglect of health care and education for the poor and the disappointments experienced in other anti-poverty programs.

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5. We support the basic framework of CAS objectives -- focus on reforming states, support for policy reforms, acceleration of human development and poverty alleviation, increased attention to social and environmental concerns, and promotion of private and financial sector development - and the overriding emphasis on selectivity linked to comparative advantage and economic performance. This approach is consistent with the overall Bank objectives contained in the Strategic Compact. However, we also see an apparent disconnect between the preliminary loan-by-loan program and the Bank's priorities as outlined, e.g., the apparent lack of financial sector or environmental projects, the willingness to maintain some lending to non-reforming states, and the absence of defined Bank activity in such critical areas as gender, child labor and AIDS control. We understand from staff that aggregate data may be misleading and that the lending program will focus clearly and selectively on identified development priorities and be firmly linked to performance. We expect this will be the case and that the link between development priorities and the actual lending program will be far more explicit. Unlike the precision we have seen in other recent CAS documents, the discussion of alternative lending scenarios (paragraphs 64-65) also appears vague.

6. On a related format issue, we liked the idea behind Box 1 on page 9 -- stating a monitorable vision for the Bank over the medium- and long-term, although it would have been helpful to establish a clearer linkage between a lending program, focused very heavily on power and transportation, and the human resource indicators that are the core of the "vision". We also wonder why no new operations are planned in the financial sector given the increased attention now being focused within the region on strengthening banking sectors.

7. The Bank Group's Strategy is heavily focused on lending to reforming states. This tactical decision strikes us as exactly right. However, as we have noted in previous discussions, lending to sub-national borrowers poses a number of unique issues and risks. We regret the delay in the Board paper on Adjustment Lending to Sub-national Borrowers and look forward to a full discussion on this important issue. In the interim, it remains crucial to ensure lending to states is structured within a good macro framework, is based on specific monitorable conditions, is reinforced by full central government support, and is very selectively tied to demonstrated state performance.

8. We have a serious problem with the plan to use the new Adaptable Program Loans (APLs) to support state power sector reform. We acknowledge the importance of addressing the major bottlenecks undermining the efficiency of the power sector. We also support efforts to encourage reform-minded state governments to accelerate reforms in this sector. Likewise, we support the underlying concept of APLs -- i.e., to pilot phased but sustained support for long term development reforms. However, we do not believe the authority delegated to management for follow-on loans when the APL was approved last September is appropriate for the pivotal and large-scale energy sector operations envisioned under the India CAS. I believe that there are several important factors which dictate the need for stronger Board oversight with standard Board approval procedures:

- First, the magnitude of the APL program commitment currently envisioned is extraordinary. The CAS tables project FY 1998-00 Bank lending for electric power and energy totaling over $1.5 billion. This understates the total level of long-term funding
which will be provided in follow-on operations through the APL mechanism, e.g., the $60 million Haryana project could entail total Bank commitments of up to $600 million.

- Second, the first program presented, for Haryana, represents a regression in the Bank’s policy with respect to lending for power in India. True, there are a number of welcome reforms in the program, including the unbundling of the state electricity board and privatization of the distribution facilities. However, the Bank — after having withheld lending to the sector because of problems that stem from the SEBs’ refusal to set tariffs for consumers in the agricultural sector at economic levels — has tabled a loan program which fails to resolve that problem satisfactorily. As a result, power will continue to be a drain on public finances in the state. Moreover, the privatization provisions are very weak. The existing power generation facilities remain under state control and although private power producers are expected to provide needed increases in capacity, there is no comprehensive plan to remove the barriers that have discouraged this in the past.

- Third, the history of the Bank’s large-scale energy lending in India is dismal, creating a strong case for close Board tracking of results, not for unprecedented delegation.

- Fourth, the special issues and risks associated with lending to states, and the pivotal role such lending — of which APLs are a prominent component — has in the Bank’s overall strategy for India also warrants standard procedures.

- Fifth, the likely pressures which the structure of the APL energy loans will place on Management to continue follow-on lending require revisiting subsequent lending.

As noted in my statement last September, “if engaged early and consulted in an open manner, the Board can — both as a whole and individually — bring significant expertise and valuable shareholder perspective to the Bank’s operations.” In this case, I believe development of India’s energy sector is sufficiently crucial and the scale of Bank support sufficiently large to clearly warrant use of our regular Board procedures for “follow-on” APLs. I ask other members for their support on this matter.

9. We strongly support proposed Bank investments in human resource development. India’s record in this crucial area is mixed, and health care and education for the poor have not received adequate attention. The challenge is enormous. Roughly half of the labor force is illiterate and tens of millions of primary-school age children are working rather than learning while women remain largely excluded from social and economic programs. This underscores the importance of more rational allocations of public sector expenditures — e.g., shifting the very high costs of water and power subsidies into effective human resource development programs. It also underscores the importance of finely targeting IDA resources for health and education to the very poor. We appreciate the funding constraints on IDA allocations to India, but believe IBRD support for investment in human resource developments would also be a good investment in India’s future.

10. We also strongly support a more pro-active Bank stance in helping the Government, and its state counterparts, to address the pervasive problem of corruption. As in many other countries, corruption imposes very heavy costs and is a major barrier to more equitable economic growth. We welcome the reference to the issue in the CAS, but feel it should be
strengthened and we urge the Bank and India to work closely in developing an ambitious, aggressive strategy to eliminate distortions and opportunities for rent seeking. We believe the Bank’s recent policy framework for helping countries combat corruption should be aggressively pursued.

11. We welcome the fact that this is a joint Bank/IFC document, but would have liked to see a more substantive discussion of IFC’s role. We also wondered at the relatively narrow focus of the strategy for private sector development (See Annex 1, Page 2). My sense is that India offers opportunities for the Bank to be both aggressive and innovative in the microcredit area, although I recognize that other donors (such as UNDP) are already active in this area.

12. We also request staff to elaborate on its approach to gender and child labor. These are referenced in the CAS but there is little discussion of these important issues. Bonded labor is another serious problem which needs increased attention. There is also little reference to Bank Group collaboration with other multilateral (ADB and UNDP) and bilateral donors. We strongly encourage maximum dialogue and operational coordination to sharpen comparative advantage, share lessons learned, and enhance impact on the ground.

13. We do not believe there should be any further decentralization of core fiduciary services to the field until the existing (already largely decentralized) procurement process is fully assessed and any weaknesses addressed. Given the Bank’s recent commitment to mainstream a discussion of the Country Procurement Assessment Report (CPAR) and an agenda to strengthen the national public procurement system into the CAS dialogue with borrowers, we are disappointed that these key areas of public sector management are not addressed.

14. I strongly commend Bank staff and their Indian counterparts for the extensive public consultations that went into the formulation of the CAS. We continue to believe that a proactive public dialogue on key development issues is a “win-win” situation, and we strongly urge the federal and state governments to make the CAS publicly available.