Center for Global Development

THE WORLD BANK'S WORK IN THE POOREST COUNTRIES: FIVE RECOMMENDATIONS FOR A NEW IDA

REPORT OF THE IDA15 WORKING GROUP
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Preface

The Center for Global Development (CGD) has taken a special interest in promoting greater effectiveness of the world's most important development institutions. In the last two years we have issued four reports that provided strategic recommendations for incoming leaders at the World Bank (June 2005), the Inter-American Development Bank (January 2006), the African Development Bank (September 2006), and the Global Fund to Fight AIDS, Tuberculosis and Malaria (October 2007). We hope to use these reports as benchmarks over time to provide independent and constructive perspectives on the progress and performance of key international institutions—some of which are under attack for lack of sufficient accountability to the communities and members they are meant to serve.

This report constitutes the fifth in what has become for us an important and we hope useful series. It is directed to the senior officials of the major donor countries that make periodic contributions to the International Development Association (IDA), the part of the World Bank that works in the poorest countries through concessional or "soft" loans and grants.

The coming months are crucial for IDA. Donor governments that give the money needed to support IDA's operations are discussing what will be its 15th replenishment. A major challenge for the new president of the World Bank will be persuading donors that increased contributions are warranted.

The discussions typically and rightly cover not only financial resources for IDA. The donors wrangle over the "vision" for IDA and the priorities they want Bank management and staff to pursue through IDA. Over the past decades, along with the billions of dollars committed, donors have added more and more recommendations, earmarks and mandates.

This report sets out five recommendations for the donor officials (the "IDA Deputies") as they discuss the next replenishment. One theme runs throughout the report: that they ought to emphasize the special role that IDA financing and accompanying expertise should play in what is an increasingly crowded donor field in many of the highly aid-dependent countries. Over the years, the ever increasing list of donor "priorities" has spread IDA thinly and now threatens its core role: filling gaps other donors neglect, especially on fundamental institutional issues such as governments' management of expenditures and the strengthening of government "systems"—of health, education, banking supervision and so on.

The report raises two other issues I want to highlight here. The first is a fallout from the Multilateral Debt Reduction Initiative (MDRI) and involves how IDA deals with the "reflows issue," that is, its loss of once-expected reflows given that countries have had their debt forgiven. At the moment, IDA "books" reflows at near 100% and commits future IDA lending on that basis. The report suggests that IDA's shareholders consider booking future reflows at much less than 100%, to avoid the moral hazard created and the risk of future "defensive lending" to ensure those reflows.

The second is the need to give the countries that are recipients of IDA, but have no formal role in the policy-setting process of the replenishments and limited control over its deployment, more voice and representation. Surely the Bank's work via IDA would be more legitimate and effective with greater involvement of the poorest countries in setting IDA priorities.

The recent turmoil at the World Bank that ended with President Wolfowitz's resignation has raised the profile of the replenishment discussions, and some observers worry that commitments will be affected by the controversy. Backing away from IDA, especially at this time, would be a mistake. The world needs a strong IDA, and it will have one if Deputies follow this report's recommendations.

I thank my colleagues Dennis de Tray and Todd Moss (who has recently become a senior official in the United States' State Department), and the members of the working group they convened for producing this thought-provoking report in a timely way. I commend the report to the IDA Deputies and hope they will find it helpful as they struggle with IDA's future.

The working group report was made possible by support from the William and Flora Hewlett Foundation, and The John D. and Catherine T. MacArthur Foundation. As always, we are grateful to our founding chair Edward W. Scott, Jr. for his support of our work, and to our other funders for their contributions to our mission to improve policies and reduce global poverty and inequality.

Nancy Birdsall
President
June 2007

Executive Summary

The International Development Association (IDA) is the premier multilateral institution serving the world's poorest countries. As they do every three years, in March 2007, Deputies representing the donor nations that fund IDA met to begin discussions on IDA's future. These negotiations will continue throughout this year and possibly early next year. They will determine IDA's 15th replenishment, and will set its course as a development institution for three years beginning July 2008.

As part of its work on the effectiveness of multilateral institutions, the Center for Global Development brought together a group of individuals knowledgeable on IDA, on multilateral institutions, and on development and asked them to consider the key issues on which Deputies need to focus if IDA is to maximize its effectiveness in helping the world's poor. The working group settled on five recommendations that should guide IDA Deputies during their discussions. These are:

As IDA Deputies prepare for the next round of discussions in Maputo, Mozambique in late June, the Working Group believes that these five "guiding principles" provide a framework for ensuring a successful replenishment round

1. **ADMIT YOU NEED IT: Affirm IDA's central role in the international aid system.** Whatever its critics say, IDA remains the hub of the international aid system for poor countries. With the international aid landscape becoming increasingly crowded, it is ever more important to have one institution with the capacity—and mandate—to coordinate, provide global knowledge, and lead donor input into country strategy setting.
2. **BEWARE THE CHRISTMAS TREE: Allow IDA to concentrate on its core roles by reserving pet issues for other agencies.** If IDA is to serve the role set out above, its strategy and work program cannot be the sum of shareholder wish lists. Shareholders must allow it to have a limited set of priorities and stay focused on delivering them.
3. **STOP PLAYING POLITICS: Don't hold IDA hostage to broader geopolitical battles.** Every IDA replenishment has its squabbles, but this year's negotiations are particularly clouded. IDA is too important for Deputies to let short-term disagreements degenerate into long-term negative consequences for IDA. This includes fully funding the 15th replenishment at a size commensurate with IDA's role and importance.
4. **GET SERIOUS ABOUT FRAGILE STATES: Push IDA to find the right incentives for dealing with the toughest countries.** IDA's strategies to promote development in recipient countries have evolved significantly over time, but many of the innovations have been driven by the better performing countries. IDA must find a way to work in difficult governance settings that preserves its credibility but is also realistic about what can be achieved.
5. **SHARPEN THE INCENTIVES FOR PERFORMANCE: Build on the current allocation system to strengthen the link to results and good governance.** The link between performance and resource allocation sets IDA apart from many other agencies and must not be weakened. However, IDA Deputies should consider ways of strengthening the incentives the system produces by steepening the performance-allocation curve, simplifying the Country Performance and Institutional Assessment (CPIA) process, helping

countries to understand the system, and creating a secondary output-based CPIA for fragile states.

As IDA Deputies prepare for the next round of discussions in Maputo, Mozambique in late June, the Working Group believes that these five “guiding principles” provide a framework for ensuring a successful replenishment round. But perhaps the main constraint that may keep IDA from delivering on its critical agenda is its governance structure. At the moment, recipient countries have almost no meaningful input into a process that is, in principle, addressing their home-grown needs. In today’s world, this is neither acceptable, nor practical. IDA does not need to be fully democratic, but it does need real recipient country participation.

The World Bank's Work in the Poorest Countries: Five Recommendations for a New IDA

In July 2008, the International Development Association (IDA) will enter its 15th replenishment period. As they do every three years, Deputies representing the donor nations that fund IDA will engage in a series of meetings throughout 2007 to decide on IDA's future. In a world increasingly critical of the inefficiencies and duplications in the delivery of foreign assistance, the Deputies' most critical challenge during these discussions may be less about "how much" and more about "how best to help." IDA's commitment level for the 15th replenishment period, important as it is, is less important than ensuring IDA's position as the lead development agency working in poor countries.

IDA's commitment level is less important than ensuring IDA's position as the lead development agency working in poor countries

This report summarizes the deliberations of a Working Group organized by the Center for Global Development as part of its ongoing effort to improve the effectiveness of the multilateral system. It begins by laying out the context and issues that influenced the group's thinking and then turns to five recommendations for the IDA Deputies as they continue their negotiations in June. The report offers an agenda that, if adopted, will ensure that IDA remains the leading agency in the provision of development assistance to poor countries and will put it at the forefront of efforts to reform the international aid business.

A new world development order…

When it was created in 1960, IDA faced a global context dominated by Europe's newly independent colonies, divided by escalating Cold War competition between the West and the Soviet Bloc (see Annex A). Today, IDA must work in a world in which growing interdependence links poverty in the developing world with security in the developed world, and in which global public goods, health and climate change among them, know no national boundaries. As IDA and its operations come under scrutiny as never before, shareholders must not forget: the world needs an effective IDA today even more than it did in 1960.

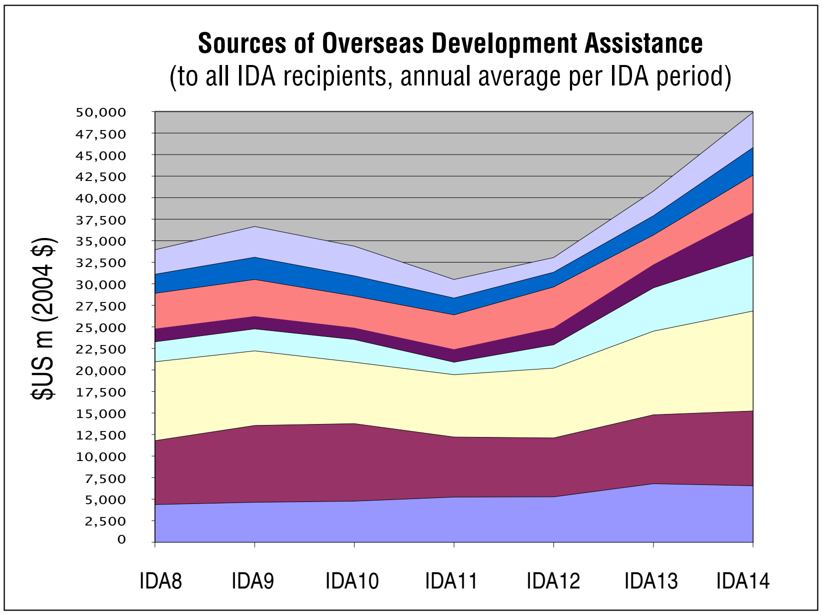
…where the aid industry has exploded

For much of its existence, IDA was the dominant donor in most of the countries in which it operated, but over time the aid field has become increasingly crowded. In 1960 the average recipient country had to deal with about a dozen donors. Today that number is over 30. The Organization for Economic Co-operation and Development (OECD) puts the total number of international development organizations or programs at over 230, with more than 100 of these working in the health sector alone.[1] Despite innumerable conferences, studies, declarations and admonitions, there is little evidence that donor harmonization and coordination is improving, and some evidence that project proliferation is worsening.[2]

While IDA's annual disbursements have grown, bilateral aid programs have grown faster

While IDA's annual disbursements have grown from about $4-5 billion during IDA11 and 12 to $6-7 billion in IDA13 and 14, bilateral aid programs have grown faster (see Figures 1 and 2). Growth in specialized funds, especially in health, is also outstripping growth in broad-based development assistance (Figure 3). Adding to IDA's changing world, a number of new, "emerging" non-Development Assistance Committee (DAC) donors are entering the development fray. China is the largest of these, but the donor involvement of India, the Arab states, South Korea, Brazil and other countries is also on the rise.

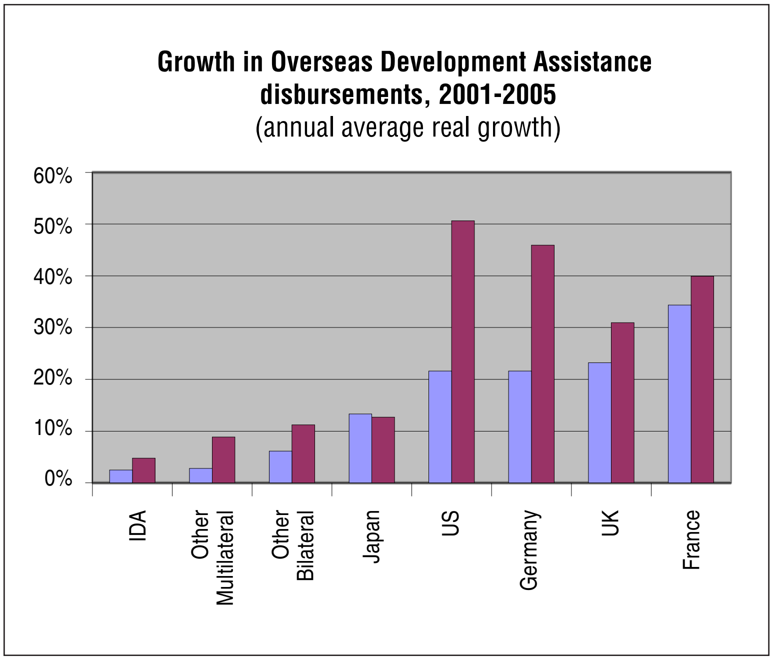
Figure 1 IDA hasn't kept pace with other sources of aid…



[1] World Bank (2007), "Aid Architecture: An Overview of the Main Trends in Official Development Assistance Flows," International Development Association, Resource Mobilization, February.

[2] David Roodman (2006a), "Aid Project Proliferation and Absorptive Capacity," Working Paper 75, Center for Global Development, January; (2006b) "Competitive Proliferation of Aid Projects: A Model," Working Paper 89, Center for Global Development, June.

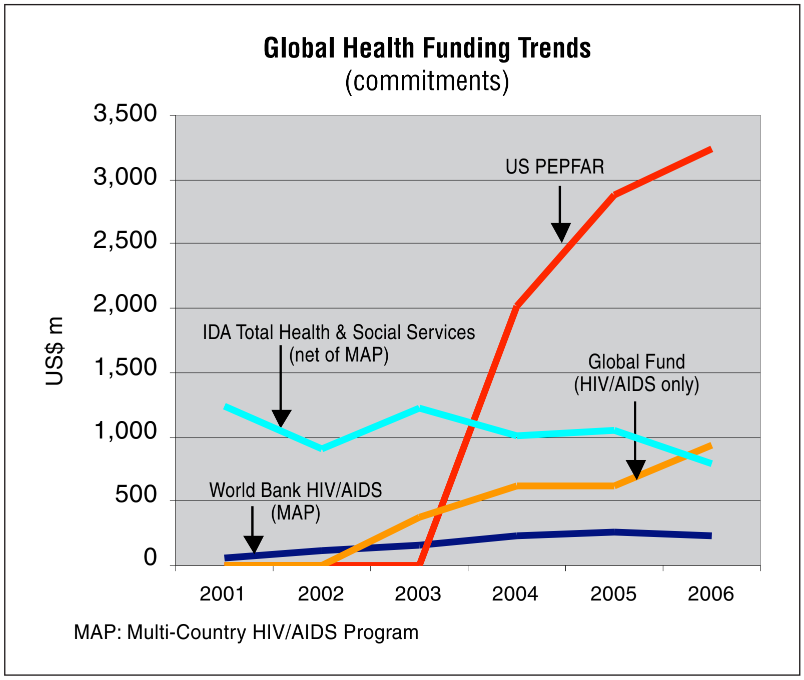
Figure 2 …Especially in recent years



Any shift of shareholder resources away from IDA could be seen as a vote of no confidence

Total global aid has doubled since 2000, to above $100 billion in 2005 and 2006. This massive increase is in one sense a positive sign in that it demonstrates a renewed international commitment to the problems of the global poor. But it also presents challenges to IDA. Any shift, absolute or relative, of shareholder resources away from IDA could be seen as a vote of no confidence by some shareholders. IDA does not have to be the biggest player everywhere, but a shrinking share globally could jeopardize its role in the international donor system.

Figure 3 More for HIV/AIDS, less for systems



Note: 2006 figures for PEPFAR and the Global Fund are estimates from CGD's HIV/AIDS Monitor.

In the not-too-distant future, IDA will be left with a client base of smaller, poorer countries in which it and the international community have had little success

…where IDA's price of success is a tougher client base

To date, 23 countries have graduated from IDA, including China. Indonesia is expected to join this group during the IDA15 period, and India, IDA's single largest client for more than a decade, in the next 5-10 years (see Table 1). In the not-too-distant future, IDA will be left with a client base of smaller, poorer countries in which it and the international community have had little success in producing sustainable growth and poverty reduction. Out of the 82 IDA-eligible countries, nearly half are now classified as weak or fragile states, meaning they lack the basic institutions and governance needed to serve their citizens (Annex C). While bilateral agencies can be selective in their client bases, IDA is expected to work in all its member countries.

…where "multilateralism" is needed as never before

IDA is a global public good. Much of the international aid system relies on IDA to provide coordination on key issues and programs, basic work on country-level strategy and financial management, and research on critical development issues. These roles have been the rationale for substantial financial and political support for nearly half a century, and they continue to be valid today. They are, however, being challenged.

- The rise of large vertical funds such as the Global Fund for AIDS, Tuberculosis and Malaria, the growing presence of philanthropists and increased levels of bilateral assistance could be taken as signaling a decline in IDA's importance. In fact, they point to the need for a stronger IDA that delivers the "foundation"—the policies, systems, human resources and institutions—on which others rely. Much of what IDA provides is easily overlooked…until it is not there.

- At the same time, the multilateral nature of IDA and its diverse shareholder base mean that it is constantly subjected to requests to do more, tackle every new problem and address each new objective. An IDA that is the sum of shareholder parts is an IDA stretched over too many objectives, and focused on none.
- For better or worse, the triennial replenishment discussions are one of the rare times when rich countries talk about development policy and approaches with money on the table. Because of this, IDA replenishment negotiations have at times been the site of ideological and political battles over a host of issues, the outcomes of which have left IDA staff struggling to find a way forward.

…where unfulfilled global promises could lead to pressure for quick-fixes
At some point in the IDA15 period, it will become obvious that many developing countries will not reach the Millennium Development Goals. When this happens, new and old questions are likely to arise about aid effectiveness and the wisdom of existing commitments to scale up aid. IDA itself may come under attack for failing to live up to expectations. This may lead to pressure to spend in areas that yield quick returns, that are easily measured and thus politically salable. We argue below that this "quick fix" mode of operation is not the role IDA should play in today's world.

IDA has the expertise, experience and credibility to coordinate, provide global knowledge, and lead donor input into country strategy setting

RECOMMENDATIONS OF THE WORKING GROUP TO THE IDA DEPUTIES

The changing global context and IDA's special role in the aid delivery system suggest that IDA Deputies would do well to focus on the following issues as they consider their options during the replenishment negotiations:

1. ADMIT YOU NEED IT: Affirm IDA's central role in the international aid system

Whatever its critics say, IDA remains the hub of the international aid system for poor countries. With the international aid landscape becoming increasingly crowded, it is ever more important to have one institution with the capacity—and mandate—to coordinate, provide global knowledge, and lead donor input into country strategy setting. This is a role that cannot be played by bilateral agencies. Among multilateral agencies, IDA has the expertise, experience and credibility to do so.

IDA brings to the development table an ability to integrate ideas and strategies across sectors, across countries, and across the donor community. Bilateral donors, especially vertical funds, tend to focus on particular problems or sectors driven by constituencies or mandates. IDA, in contrast, has an overview of all the key sectors, which position it to help countries make tradeoffs and exploit complementarities. Similarly, most donors engage selectively in countries based on historical, political or other criteria. IDA is involved in most countries and thus is well placed to promote cross-country programs.[3] Finally, IDA is well situated to be the main interlocutor between donors and recipient country governments, so long as the other players give it the authority to do so.

This means that IDA's lending and grant levels do not capture its full value to the international aid system. Its most important contribution may well be what it does beyond the money. If IDA is to be effective in this non-financial role, it will have to focus on building and working with country systems, rather than project financing, which often bypasses these systems. Such an approach implies a heavy concentration on country-level strategies that integrate cross-sector linkages, local capacity building for budget management, practical systems for service delivery, and the creation of the basic information needed by all actors to work efficiently—and for citizens to hold their governments accountable. IDA's primary role must be to help build the systems that let other donors use their money well.

IDA's primary role must be to help build the systems that let other donors use their money well

IDA is, fortunately, already moving in this direction in some sectors. The recent World Bank Health, Nutrition and Population strategy represents a shift in mindset, where IDA's focus will be on improving health systems in order to increase the absorption and sustainability of the growing number of often single-issue global health initiatives (see Box 1).[4] Under this new approach, IDA will not fund antiretrovirals but will help countries set their own health strategies and systems so that they can better spend money from the Global Fund, the US President's Emergency Plan for AIDS Relief (PEPFAR), the Gates Foundation, bilateral agencies, and the hundreds of official and private organizations involved in global public health.

Deputies now should urge IDA to adapt this strategy to other sectors as it builds on its comparative advantage relative to other development actors. Rather than build schools or buy textbooks, IDA should work with governments to strengthen education systems that make better use of the resources other donors are committing to schools and books. Rather than build roads and bridges, IDA should focus on the policies and institutional structures that will attract private capital where that makes sense and help to mobilize public money where needed. These institution-building goals will take time and patience on the part of both donors and recipient countries.

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[3] In fact, a recent World Bank study found IDA's regional programs to be highly effective; see World Bank (2007), "The Development Potential of Regional Programs: An Evaluation of World Bank Support of Multi-country Operations," Independent Evaluation Group.

[4] World Bank (2006), "World Bank Strategy for Health, Nutrition and Population Results," May.

Box 1

Getting it Right in Health: A model for other sectors?

Driven by a proliferation of new health funds and a concern that the outcomes of its past health interventions are largely unknown, the World Bank is making a concerted effort to identify and establish its role within the health sector.[5] The new strategy begins with the notion that the World Bank has the largest reach, the most experience and resources, and a unique ability to work in ways that no other institution can. The Bank's size allows it to work…

- **Across Sectors.** The World Bank's breadth of focus allows it to cover the whole country rather than limited sectors or specific issues. It can coordinate complementary sector interventions that have perhaps indirect but nonetheless integral implications for health. For instance, supporting infrastructure investments improves access to clean water and clinics, and helping design policies to manage the impact of demographic change can help governments prepare for future demand shocks for health services.
- **Across Countries.** Because the World Bank works in many countries it can more easily coordinate regional programs. It also can play a key role in generating global and regional public goods, particularly information and its dissemination. Bank-coordinated cross-country impact evaluations, for instance, provide valuable policy-relevant knowledge to other countries and donors who are designing and planning health interventions.
- **Within Systems.** The World Bank is the donor best situated to tackle health systems improvements within a country. The Bank's capacity to link the health sector to broader macroeconomic and budgetary issues, advise governments on strategizing health priorities, and coordinate the variety of investments necessary to build functioning, sustainable health systems is unique among donors. These systemic interventions help maximize the impact of other donors' disease-specific interventions.

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[5] Ruth Levine and Kent Buse (2006), "The World Bank's New Health Sector Strategy: Building on Key Assets." *Journal of the Royal Society of Medicine*. Vol. 99; and Alex Shakow (2006), Global Fund-World Bank HIV/AIDS Programs Comparative Advantage Study. The World Bank and the Global Fund.

2. BEWARE THE CHRISTMAS TREE: Allow IDA to concentrate on its core roles by reserving pet issues for other agencies

If IDA is to serve the role set out above, its strategy and work program cannot be the sum of shareholder wish lists. Shareholders must allow IDA to set priorities and focus. IDA's diffusion over the years stems in part from shareholders' desires to shape IDA in the image of their national development goals. But it is also a result of the international community turning too often to IDA to respond to emergencies and special needs. Both need to stop. Bilateral agencies should use their own resources to pursue special interests, and the world is replete with agencies set up to deal with emergencies.

Shareholders must allow IDA to set priorities and focus; bilateral agencies should use their own resources to pursue special interests

If Deputies are serious about focusing IDA on critical foundation-building challenges, it will have to:

- Make clear in the IDA15 agreement IDA's role in the international aid system. This statement must be specific enough to provide for monitoring and evaluation and to avoid future wrangling among shareholders.
- Agree to stop adding new areas for IDA to tackle. If there are pressing new issues or ways of operating that a shareholder prefers, save those ideas for the bilateral agencies or the relevant specialized international agencies, including the various arms of the United Nations.
- Perhaps most important, agree on what IDA will *not* do. This conversation should be driven by the basic principle that IDA stay out of areas where others are already established or have specialized expertise. This would allow IDA to concentrate on its strengths, and let it lead the way in clarifying the international division of labor needed to reduce overlap and contradictory mandates.

Deciding what IDA will not do is going to be difficult. While individual country conditions must be the primary guide for development strategies, Deputies could provide guidance on areas in which IDA should seek to avoid operational engagement (the one exception is knowledge work, which would have to be broad-based if IDA is to have credibility in leading and informing strategy discussions). Among areas that could be on a proposed "negative" or "low priority" list are:

- Emergency relief
- "Rapid response" to natural and other catastrophes
- Immediate post-conflict programs, beyond budget and financial management
- Project financing for social services
- Direct "brick and mortar" financing

To be successful in refocusing IDA, Deputies will have to deal with two issues that could derail these efforts. The first is the "it's too important for IDA not to do" syndrome. Taking something off IDA's agenda cannot not be seen as taking it off the international assistance agenda. The second is the need for a serious rethinking of the incentive structure for IDA staff if they are to focus on institution and capacity building. As we argue below (Recommendation 5), a new measuring rod will have to be developed if IDA is to be held accountable for progress along the "long march" of institution building.

3. STOP PLAYING POLITICS: Don't hold IDA hostage to broader geopolitical battles

Every IDA replenishment has its squabbles, but this year's negotiations are particularly clouded by tensions between IDA leadership and some key shareholders, and between shareholders themselves. IDA is too important to the effectiveness of international development assistance for Deputies to let short-term disagreements degenerate into long-term negative consequences for IDA.

Deputies must not let short-term disagreements degenerate into long-term negative consequences for IDA

The Working Group welcomes the Executive Board approval of the World Bank's governance and anti-corruption strategy, and hopes that it marks the beginning of a constructive debate on how IDA can address these critical issues. It is also a good sign that many of the most contentious issues from IDA14, such as grants, appear resolved and have not spilled over to the current round (see Annex B). We strongly urge the Deputies to refrain from using the IDA discussions as a forum for contesting broader development strategy and tactics, where consensus may be elusive, and to fully fund the core competencies where consensus is already emerging.

The Working Group does not make a specific funding level recommendation for the replenishment round, but does offer the following guidelines:

- *Match funding to responsibilities.* IDA's size must be commensurate with its role as the agency tasked with ensuring that the sum of a country's development assistance is greater than its parts. A reduced IDA will not have the critical mass needed to continue to play these foundational roles. The extra financing required to compensate for recent debt relief is a real issue for IDA, but there are both optimal and practical solutions that can be found (see Box 2).
- *Recognize that political signals matter.* If the shareholders continue to believe that IDA is a vital institution then the allocation of resources must signal that support. A declining share of IDA in an age of rapidly expanding global aid flows could be seen as a vote of no or low confidence.
- *Keep IDA's effectiveness in mind.* While IDA could do better in measuring its impact, it is still the best development agency when it comes to tracking what it does and the effects of its programs. Because of that, IDA often comes under a significantly higher level of scrutiny than any of the other agencies and programs. In assessing IDA's performance, Deputies need to ensure that the same standards are being applied in assessing IDA's merits.

Box 2

Filling the debt relief "hole" in IDA finances: Making sure the perfect is not the enemy of the good

There are concerns that recent debt relief agreements will reduce IDA's financing ability. In particular, an IDA paper claims that there is a $10 billion shortfall as a result of the combined Heavily Indebted Poor Countries (HIPC) initiative and the Multilateral Debt Relief Initiative (MDRI).[6] On face value this appears broadly correct, taking into account the lost reflows from forgiven obligations up to 2019. Shareholders should fulfill their promises from the MDRI negotiations to compensate IDA on a "dollar for dollar" basis. But, as these negotiations go forward, Deputies need to keep in mind that:

- Any shortfall in the replenishment of "lost reflows" from HIPC countries would be offset by a reduction in new commitments to the countries that receive debt relief; *net* flows to these countries would not be affected. Even in a worst case scenario in which the entire shortfall remains unfunded by donors, *gross* disbursements will decline by the full amount of the debt service savings, but the net transfers from IDA to recipient countries will remain unchanged.

- There is, however, another complication arising from what IDA calls its "advanced commitments." By this scheme, started during the IDA8 period, IDA makes current commitments based on the expectation of reflows up to ten years into the future. Debt relief has thus created two immediate problems: (1) reflows expected to come in during IDA15 can no longer be advance-committed since the reflows have now been forgiven; and (2) some of the forsaken future reflows have already been committed to other countries.

- Given these potential financing issues, the donors have all promised to compensate IDA "dollar for dollar" to make up for these lost reflows. This was part of the final MDRI agreement in which each donor signed an "instrument of commitment" pledging to cover their shares. But even with this signed commitment, IDA is seeking additional guarantees on these pledges. Some countries have been able to back their commitments with parliamentary approval; other countries, notably but not only the United States, do not and cannot pre-appropriate funds. US contributions to IDA have always been committed for a three-year replenishment period but appropriated by Congress on an annual basis. IDA is now asking the US to authorize or appropriate for the full ten years to enable them to advance commit that future money. (Thus, in an irony of history and a result of IDA's accounting system, the future debt payments from countries like Benin and Niger had been scored by IDA at nearly 100 cents on the dollar, but future US commitments are scored at zero.)

The ideal solution: Each of the donors should provide IDA a guarantee to circumvent any possible interruption in financing from the debt relief initiatives. This would include legislative authorization, if not appropriation, to avoid any future uncertainty. All of the shareholders should pursue this option to the fullest extent possible.

One practical solution: In practice, however, national budget rules for the US and others are unlikely to change to accommodate IDA. It would make sense, therefore, for IDA to find a compromise, working with the commitments that shareholders are able to provide. This may mean counting, at some reasonable discount rate, the existing instruments of commitment. (If Benin's loan obligations can be counted at 95%, then surely the US pledges can be at some rate well above zero.) IDA will, however, first need to be more transparent and forthcoming about the true marginal impact on its operations from the lost capacity to advance commit funds from the handful of donors who cannot provide multi-year ironclad guarantees.

Plus, a prudent fix for the future: Whatever solution is found, this is a good time to revisit the advance commitments arrangement, since it may not be prudent to continue the scheme in its current form. Pre-committing funds from future repayments creates moral hazard, including strong incentives for defensive lending that undermines the ability of IDA to be selective in the future. Some reform of the advanced commitments scheme, even if it is just a simple reduction in the ratio of total reflows allowed to be pre-committed, would be advisable.

[6] World Bank (2007), "IDA's Long-Term Financial Capacity," International Development Association, Resource Mobilization, February.

4. GET SERIOUS ABOUT FRAGILE STATES: Push IDA to find the right incentives for dealing with the toughest countries that may matter most

Today's greatest challenges to global prosperity and security come from lack of development—that is progress toward stable, accountable national institutions that can meet citizens' needs and fully participate in the workings of the international community. IDA's strategies to promote development in recipient countries have evolved significantly over time, but many of the innovations have been driven by the better performing countries. Because countries that score well on the current Performance-Based Allocation (PBA) system, such as Tanzania, Honduras and Georgia, get more resources and are higher profile, they also tend to attract the best staff and most attention from headquarters. While this is consistent with the intent of the PBA system, it conflicts with the growing demand for IDA to increase its effectiveness in weak and fragile states. The increased attention to sub-Saharan Africa is one example of this pressure, but there are many fragile states in other parts of the world, eight in East Asia, for example (see Annex C). IDA must develop an effective means of working globally in difficult governance settings that preserves its credibility but is also realistic about what can be achieved.

IDA must develop an effective means of working globally in difficult governance settings that preserves its credibility but is also realistic about what can be achieved

The guiding principles for engaging in these countries have progressed considerably and should be given time to work and be tested.[7] However, even if the thinking has advanced, IDA needs to deal more aggressively with three issues:

- *Staff incentives.* A recent proposal for boosting fragile states capacity and the incentives for staff to work on these difficult countries is a good starting point and should be supported.[8] But clear performance benchmarks need to be set out that allow IDA to determine if the program is working—that is, getting the right staff to work on the toughest countries. More concrete rewards may well be needed beyond promises of future advancement. A review of the impact of these measures within 18 months and consideration of enhanced incentives would be warranted.
- *Risk incentives.* The diversity of countries in the fragile states classification means that interventions have to be tailored to country conditions. Rather than formulating a central strategy, IDA must continue to pioneer new approaches and mechanisms to gain traction in the toughest cases. It should find ways to encourage innovation and risk-taking with rigorous evaluation of interventions. Creative ideas—output-based aid, "payment for progress,"[9] developing better intermediate indicators, and others—need to be tried and assessed if IDA is to improve its track record in these countries.

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[7] Development Assistance Committee (2006), "Fragile States: Policy Commitment and Principles for Good International Engagement in Fragile States and Situations," Development Co-Operation Directorate, DCD/DAC(2006)62, November.

[8] World Bank (2007), "Strengthening the World Bank's Rapid Response and Long-Term Engagement in Fragile States," Operations Policy and Country Services, Fragile States Group, January.

[9] Owen Barder and Nancy Birdsall (2006), "Payments for Progress: A Hands-Off Approach to Foreign Aid," Working Paper 102, Center for Global Development, December.

- *Country incentives.* IDA still has relatively weak tools for encouraging low-performing countries to improve. More creative analysis, including taking political economy constraints more fully into account at the country level, should be a priority for IDA, as well as finding ways to create incentives for countries to increase performance (see Recommendation 5 below for one such suggestion).

5. SHARPEN THE INCENTIVES FOR PERFORMANCE: Build on the current allocation system to strengthen the link to results and good governance

The link between performance and resource allocation sets IDA apart from many other agencies and must not be weakened. However, IDA Deputies should consider ways of strengthening this system, including the following:

The allocation formula weighting for performance should be steepened to increase the rewards of good performance

- *Steepen the PBA curve.* The current system does allocate more resources to top-performers than those in the middle, but the differences—especially in a world of multiple aid donors using their own (usually inexplicable) allocation systems—are typically not great enough to reward countries for good performance. Moreover, the complex nature of the allocation system, and the many elements of "performance" mean that improvements in one area may not yield additional resources commensurate with the political risks involved. The allocation formula weighting for performance should be steepened to increase the rewards of good performance.
- *Simplify the CPIA.* Ongoing work to reform the CPIA scoring system should be encouraged, but current proposals to alter the formula weightings do not go far enough.[10] For the index to have its intended effect, countries must be able to understand where the numbers come from, how they are calculated, and what must be done to change them. The fact that all of the CPIA is based on internal Bank data—and much is based on the subjective judgment of Bank staff—prevents the PBA system from working as well as it could. Proposals for replacing some parts of the index with objective or externally-generated indicators should be given serious consideration.[11]
- *Work with countries to understand the system.* The US Millennium Challenge Account (MCA), which uses an index of external indicators to determine program eligibility, has helped to create incentives for performance through its "threshold program." This initiative is a deliberate effort to work with countries to help them understand their scores and formulate strategies for improvement.[12] IDA should strengthen its program to help countries understand the CPIA and link the indicators to strategies for raising their scores.

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[10] World Bank (2007), "IDA's Performance-Based Allocation System: Options for Simplifying the Formula and Reducing Volatility," International Development Association, Resource Mobilization, February.

[11] Ravi Kanbur (2005), "Reforming the Formula: A Modest Proposal for Introducing Development Outcomes in IDA Allocation Procedures," Centre for Economic Policy Research, Discussion Paper No. 4971, March.

[12] See MCA Monitor on www.cgdev.org, including Steve Radelet, Sarah Lucas and Rikhil Bhavnani (2004), "2004 MCA Threshold Program: A Comment on Country Selection," Center for Global Development, October.

- *Develop a modified "CPIA-F" for low performers and fragile states.* The incentives within the current CPIA system are especially weak for countries at the bottom of the spectrum because changes in the CPIA are often linked to difficult institution-building agendas. The combined effect of averaging across many indicators and the use of relative levels means that there are typically only small benefits from feasible increases in CPIA scores for weak and fragile states. For these countries, IDA should explore alternatives that would create clearer and stronger incentives for starting and staying with the long-term process of building institutions and capacity. One approach would be to create a "CPIA-F," a second index for this category of fragile countries to allocate a pool of resources. This would have to be a much simpler index that measures performance changes in a set of easily tracked outcomes. This is not in and of itself an argument for more resources to fragile states. It is a proposal for developing a more appropriate and effective system for allocating resources within this group.

Conclusion: The unavoidable issue of IDA's governance

As the IDA Deputies prepare for the next round of discussions in Maputo, Mozambique in late June, the Working Group believes that these five "guiding principles" provide a framework for ensuring a successful replenishment round. But perhaps the main uncertainty hanging over IDA's future is its governance structure. At the moment, recipient countries have almost no meaningful input into a process that is supposed to address their home-grown needs.

As a development agency, full democratic representation is neither realistic nor desirable, but the current system undercuts a fundamental starting point for IDA's business model: country ownership. The notion that a few borrower country observers substitute for real representation is just not credible. IDA's shareholders need to have a serious discussion about how IDA's current governance structure is working—or not. Ideally such a discussion will lead to a request by the Deputies to the World Bank staff for analysis of the implications of the current structure and reform proposals for consideration within the next few years.[13]

Deputies must bring IDA's role, responsibilities, and ownership in line with the 21st century. If it is to remain in the forefront of efforts to fight global poverty, it must have a clear mandate and strategic vision. It also must have real and appropriate representation by the countries it serves.

IDA's shareholders must have a serious discussion about how IDA's current governance structure is working—or not; recipient countries have almost no meaningful input into a process that is supposed to address their home-grown needs

[13] See Nancy Birdsall and Devesh Kapur (co-chairs, 2005), "The Hardest Job in The World: Five Crucial Tasks for the New President of the World Bank," A CGD Working Group Report, Center for Global Development, June.

Table 1

Top IDA Recipients

Annual average, $US millions (current)

	IDA9 FY1990-1992		IDA10 FY1993-1995		IDA11 FY1996-1998		IDA12 FY1999-2001		IDA13 FY2002-2004		IDA14 FY2005-2006*	
1	India	856	India	1,104	India	1,093	India	681	India	1,005	Pakistan	841
2	China	509	China	857	Vietnam	416	Bangladesh	491	Pakistan	609	India	819
3	Tanzania	228	Pakistan	343	Bangladesh	402	Vietnam	408	Congo, Dem. Rep.	563	Vietnam	733
4	Kenya	214	Bangladesh	317	China	366	Uganda	224	Vietnam	531	Tanzania	553
5	Bangladesh	195	Ghana	246	Côte d'Ivoire	300	Zambia	194	Bangladesh	467	Bangladesh	531
6	Ghana	190	Côte d'Ivoire	234	Pakistan	239	Senegal	178	Tanzania	368	Ethiopia	477
7	Uganda	167	Zambia	204	Kenya	188	Honduras	174	Nigeria	326	Nigeria	376
8	Pakistan	146	Uganda	189	Cameroon	161	Madagascar	170	Ethiopia	311	Ghana	335
9	Mozambique	136	Ethiopia	188	Zambia	159	Mozambique	169	Uganda	259	Africa regional	310
10	Malawi	112	Tanzania	183	Ghana	142	Yemen	156	Ghana	237	Uganda	281

*2 year average

Source: World Bank

Annex A: About IDA

IDA is the soft-loan window of the World Bank Group which makes loans and grants to the world's poor countries. Since its launch nearly five decades ago, IDA has grown to become not only one of the largest sources of development finance but also a generator and storehouse of expertise. It is, by most accounts, the single largest source of development knowledge and a driver of many of the ideas and trends that shape the global agenda. The evolution of thinking about how to promote development—from large infrastructure, to basic needs, to structural adjustment, to the emphasis on governance and institutions today—has in large part emanated from the World Bank and IDA in particular. The types of instruments IDA uses has also changed from simple loans and technical assistance in the beginning to a wide range of products today aimed to meet the varying needs of its diverse client base. But development strategy has always been—and remains today—highly controversial and marked by deep philosophical and tactical differences. IDA has frequently been a forum for those debates, and its operations often reflect the tensions inherent in both its complicated mission ("a world free of poverty") and its multilateralism (it has 165 member governments).

Annex B: A summary of the IDA14 agreement

As part of the IDA14 replenishment process, the Deputies made a series of recommendations that fall into five broad categories.

1. *Growth.* IDA strategies should place appropriate weight on economic growth as a driver of poverty reduction and include a focus on private sector development as an engine of growth.
2. *Private sector development.* IDA, in partnership with other World Bank Group institutions and external partners, should strengthen its non-lending work (including analytics, diagnostics, technical assistance and training) to strengthen the private sector in IDA countries.
3. *Increased grant allocation system.* Grants are to be increased to account for approximately 30% of IDA14 resources and distributed based on a country's risk of debt distress.
4. *New results measurement.* IDA should strengthen its performance monitoring of both country outcomes and IDA's specific contribution.
5. *Donor coordination.* IDA should work with other donors to ensure greater harmonization.

Annex C: IDA Countries

Africa

Angola ‡
Benin◊
Burkina Faso◊
Burundi◊‡
Cape Verde
Cameroon◊□
Central African Republic◊‡
Chad◊‡
Comoros◊‡
Congo, Dem. Rep.◊■
Congo, Rep.◊‡
Côte D'Ivoire◊‡
Ethiopia◊
Eritrea◊‡
The Gambia◊‡
Ghana◊
Guinea◊‡
Guinea-Bissau◊‡
Kenya
Lesotho
Liberia◊■
Madagascar◊
Malawi◊
Mali◊
Mauritania◊‡
Mozambique ✧
Niger◊□
Nigeria‡
Rwanda◊□
São Tomé and Principe◊‡
Senegal◊
Sierra Leone◊‡
Somalia◊‡
Sudan◊■
Tanzania◊
Togo◊‡
Uganda◊
Zambia◊
Zimbabwe*‡

East Asia

Cambodia‡
Indonesia*
Kiribati
Laos, PDR‡
Mongolia□
Myanmar‡
Papua New Guinea*‡
Samoa
Solomon Islands‡
Timor-Leste‡
Tonga‡
Vanuatu‡
Vietnam

Europe and Central Asia

Albania*
Armenia
Azerbaijan*
Bosnia-Herzegovina*
Georgia□
Kyrgyz Republic◊□
Moldova
Montenegro *
Serbia*■
Tajikistan□
Uzbekistan*‡

Latin America and Caribbean

Bolivia*◊
Guyana◊
Haiti◊■
Honduras◊
Nicaragua◊
Dominica*
Grenada*
St. Lucia*
St. Vincent and the Grenadines*

Middle East and North Africa

Djibouti‡
Yemen, Rep.□

South Asia

Afghanistan■
Bangladesh
Bhutan
India*
Maldives
Nepal◊□
Pakistan*
Sri Lanka

* Blend countries
◊ HIPC countries
‡ Fragile states
■ Post-conflict
□ Other countries (reviewed by World Bank Fragile States group)