G-20 Working Group 4

The World Bank and other Multilateral Development Banks

FINAL REPORT

March 2009

G-20 WORKING GROUP 4 REPORT

Executive Summary

G-20 members express concern over the sharp fall in capital flows to emerging markets. The reduction in credit availability has generated a significant economic impact on emerging markets and low-income countries (LICs) as businesses and households find it difficult to access finance. This may hamper progress towards achieving Millennium Development Goals.

G-20 members urge the multilateral development banks (MDBs) and other international financial institutions (IFIs) to step up their counter-cyclical efforts and to off-set capital flight and maintain demand by providing on a consolidated basis fiscal expansion, support to social safety nets, trade financing, bank recapitalization, and infrastructure investment in emerging markets and LICs.

G-20 members commit to use more thoroughly the resources of these institutions to bring forward global expenditure support financing to developing countries by $US100 billion over the next three years based on currently agreed capital.

They emphasize the counter-cyclical role MDBs have in support of their longer-term development mandate. They call for the MDBs, in close coordination with the IMF where appropriate, to move forward on flexible, fast-disbursing and front-loaded instruments designed to substantially and quickly assist developing countries facing financing gaps in the contect of the current crisis, in a manner that would not endanger their financial sustainability and investment ratings.

G-20 members will partner with MDBs in providing short-term financing and risk sharing and in protecting the poorest people through the crisis. They will provide additional resources for these purposes, for instance through contributions to concessional funds or new facilities.

The World Bank and the IMF should also review the application of the Debt Sustainability Framework with a view to make full use of its existing flexibility to reflect the diversity of situations across LICs.

Furthermore, G-20 members, through their involvement in the Boards of Governors, commit to urgently review the adequacy of the capital resources of all MDBs to provide appropriate increases in funding to mitigate the consequences of the crisis. Any increases should maintain appropriate safeguards and development effectiveness, and entail commitments to ongoing governance reform.

The Asian Development Bank should immediately proceed with a substantial general capital increase of 200% or $US100 billion. G-20 members, through their representatives at the Executive Boards of the African Development Bank and the Inter-American Development Bank, stand ready to initiate a review process of the capital adequacy of both institutions, at their respective 2009 Annual Meetings. The EBRD should promptly review its statutory capital constraints to give leeway to interventions by the Bank while preserving its financial strength. The Islamic Development Bank currently has a reasonable level of resources to appropriate lending growth and should continue to keep its resource needs under review in light of the evolving situation in its member countries.

G-20 members stress that MDBs' reforms should be guided by the principle of shared and common responsibility, increasing legitimacy and partnership of member countries in addressing global challenges of the 21st century.

G-20 members urge the MDBs to strengthen accountability of their management, and improving the processes to assess their performance. There is broad support from G-20 members for open, transparent, competitive, and merit-based selection process, irrespective of nationality and geographical preferences for the appointment of the senior management of the MDBs

G-20 members urge the World Bank Group to pursue comprehensive reforms of its ownership structure and internal governance. They restate their support for a full-fledged governance reform in the World Bank Group in order to increase voice and representation of emerging markets and developing economies. They call for the Development Committee at its 2009 Spring Meeting to launch a wider discussion on improving governance and effectiveness of the World Bank, and to set an accelerated timeline for the second step of the Voice and Representation reform package, with an aim to reach an agreement at the 2010 Spring Meeting. Within that process, some G-20 members call for an increase of the shares of developing countries as a whole without dilution of any individual developing member, leading over time towards an equitable voting power between developed and developing countries, while some others consider that only under-represented countries should benefit from such a measure.

Introduction

- **Mandate and purpose of the group**

The G-20 Leaders met in Washington DC on November 15th, 2008 and resolved to reform the World Bank (WB) and other MDBs, as a means to effectively counter and mitigate the effects of the ongoing financial crisis, as well as to prevent similar crises in the future. The G-20 Leaders defined the immediate action plan for reforming international financial institutions, including MDBs, by putting the emphasis on short-term crisis responses, as written in the Leaders' Declaration as follows:

  - *We should review the adequacy of the resources of the IMF, the World Bank Group and other multilateral development banks and stand ready to increase them where necessary. The IFIs should also continue to review and adapt their lending instruments to adequately meet their members' needs and revise their lending role in the light of the ongoing financial crisis.*
  - *We should explore ways to restore emerging and developing countries' access to credit and resume private capital flows which are critical for sustainable growth and development, including ongoing infrastructure investment.*
  - *In cases where severe market disruptions have limited access to the necessary financing for counter-cyclical fiscal policies, multilateral development banks must ensure arrangements are in place to support, as needed, those countries with a good track record and sound policies.*

While in the medium-term, the Leaders stated their commitment to undertake more comprehensive reform as written in the Declaration as follows:

  - *We underscored that the Bretton Woods Institutions must be comprehensively reformed so that they can more adequately reflect changing economic weights in the world economy and be more responsive to future challenges. Emerging and developing economies should have greater voice and representation in these institutions*.

- **Summary of the Working Group's approach to tackling its mandate**

WG 4 members have reviewed some immediate aspects of reform, including MDBs' mandates, adequacy of resources, instruments for counter-cyclical policies, and mechanisms to support low-income countries and the private sector during crisis periods. Furthermore, as a means to enable MDBs to respond effectively to the development challenges of the 21st century, WG 4 members have examined the broad principles and processes for wider reform over the medium-term

WG 4 members note that in the short-term the crisis affects the poorest and most fragile populations, endangering global efforts to achieve the Millennium Development Goals. In line with this, WG 4 members believe that MDBs can provide solutions to address promptly the impact of the financial crisis. WG 4 members agree that appropriate ways need to be found in order to collectively – both politically and financially – support the WB and other MDBs. WG 4 members also consider that MDBs' ability to respond effectively is closely connected with issues such as the adequacy of their capital, the issue of the scope of the MDBs' mandates and instruments. WG 4 considered that all of this needed to be fully addressed.

In its work, WG 4 focused on concrete and practical measures to address the crisis over the short-term and the medium term. In particular, WG 4 focused on measures to address the financial crisis noting they should be timely, targeted and temporary. In order to make them consistent with the MDBs' core development focus, WG 4 took the view that the measures should be aimed at supporting countries in maintaining reasonable levels of economic growth and sustaining development in the face of external shocks. Consequently, the resource requirements and instruments related to the crisis should be aligned with the MDBs' long-term strategies in a coordinated manner with other IFIs including the IMF.

- **Outreach process**

From the beginning of its working process, WG 4 has included the World Bank and the IMF as observers.

As part of an outreach process, WG 4 heard presentations and received submissions from the following MDBs: (i) the Asian Development Bank (ADB); (ii) the African Development Bank (AfDB); (iii) the Inter-American Development Bank (IADB); (iv) the European Bank for Reconstruction and Development (EBRD); and (v) the Islamic Development Bank (IsDB).

Non G-20 countries were informed and consulted through their representative at the World Bank, ADB and AfDB during meetings between co-chairs and executive boards and management.

Some non G-20 countries were consulted (Netherlands, Switzerland), as were the G-24 and the African Union, in order to better reflect the voice of developing countries. WG 4 also welcomes useful comments by the Peterson Institute for International Economics and the Zedillo Committee.

Institutional bodies and countries consulted during the outreach process were provided with all relevant working material and their comments were welcomed. Some of them (the RDBs, African Union, G-24, and the Netherlands) made direct presentations to the WG 4 members during an outreach session organized in Jakarta, back-to-back with the WG 4 second meeting on 2 March, 2009. WG 4 had first met in Paris on 29 January, 2009.

Main section

Action Plan for Reforming Multilateral Development Banks (MDBs)

The G-20 tasked Working Group 4 (WG 4) to explore ways to collectively support the World Bank and other MDBs. In addition, WG 4 was tasked to analyze the reforms required so that MDBs can effectively harness their full potential to achieve sustainable and inclusive global economic and social development.

This section sets forth a recommended work plan for MDBs to implement the principles of counter-cyclical response and reform.

The current financial crisis has affected developing countries, endangering global efforts to achieve the Millennium Development Goals. Tens of millions of people in developing countries are at risk of remaining or falling back into extreme poverty as a result of the crisis.

Developing countries – middle and low income – are finding that every source of their development financing – export and commodity demand: trade and project finance; aid flows; remittances; capital flows – has been affected by the unprecedented scale and coverage of the crisis.

G-20 members commit to working through the Multilateral Development Banks (MDBs) to provide solutions in the form of immediate increases in financing, using the full capacity of their balance sheets to provide counter-cyclical support during the crisis. In addition, G-20 members will work with MDBs to ensure that they have the instruments to counter and mitigate the effects of the financial crisis, and ensure that they are prepared to respond to future challenges.

WG 4 has reviewed some immediate constraints and strengths of MDBs, and the corresponding political and financial support they need, in order to respond to crisis effectively. WG 4 has also analyzed aspects of reform, including MDBs' mandates, adequacy of the resources, instruments for counter-cyclical policies, and mechanisms to support developing countries, in particular in low-income countries, as well as the private sector during crisis periods. In addition, as a means to enable MDBs to respond effectively to the development challenges of the 21st century, WG 4 has examined the broad principles and processes for wider reform in the medium-term.

A. Common Principles for Reform

G-20 members:

1. confirm MDBs in their legitimacy, under their mandate of *'poverty reduction, promoting sustainable development and inclusive growth',* and with an aim to foster regional cooperation, to play a counter-cyclical role to tackle crisis. Recognizing their complementary roles, MDBs should take into account their respective comparative advantages, while at the same time improving their coordination for more efficiency and minimizing overlap with both other IFIs - including the IMF - and private finance institutions; without adversely affecting the access of borrower countries to financing from different sources;

2. call MDBs to increase substantially their mobilization of resources and net transfers to developing countries in the context of the current crisis;
3. recommend the MDBs be provided with the necessary resources based on their capital adequacy under the ongoing reviews, to carry out their core mandate of development assistance in the long-term perspective as well as to cope with the crisis;
4. urge MDBs to ensure that initiatives are well coordinated and that potential borrowers or recipients are informed of new resources, instruments and procedures;
5. support a strong role for shareholders in setting out the strategic directions of the banks and agreeing on Statements of Strategic Priorities for the next few years;
6. stress that MDBs reforms should be guided by the principle of shared and common responsibility, increasing legitimacy and partnership of member countries in addressing global challenges of the 21st century. G-20 members urge the World Bank Group (WBG) to pursue comprehensive reforms of ownership structure and internal governance; and they restate their support for a full-fledged governance reform in the WBG in order to increase voice and representation of emerging markets and developing economies;
7. urge MDBs to accelerate their work on result measurements to improve performance.

Some members also:

8. call for the MDBs to continue to ensure that their business models are geared towards covering their administrative expenses, achieving cost-effectiveness for both themselves and their clients, and to maintain their potential to contribute to concessional windows to the extent permitted by their long-term financial capacity.

B. Crisis Instruments

G-20 members welcome the actions taken by MDBs to better mobilize their resources and help developing countries face the current crisis. They call for MDBs to promptly implement the following crisis response measures and report their actions by the next WB/IMF annual meeting.

B1. Regarding counter-cyclical instruments, G-20 members call for the MDBs, in close coordination with the IMF, where appropriate, to move forward on flexible, fast disbursing, and front-loaded instruments designed to substantially and quickly assist developing countries facing financing gaps in the context of the current crisis, in a manner that would not endanger their financial sustainability and investment ratings.

MDBs should:

9. advance their work to fast-track instruments and to streamline operational standard approaches and procedures, while maintaining

appropriate safeguards and ensuring development effectiveness. However, all measures adopted specifically to address the current crisis should be reviewed;

10. reinforce or expand their:
    - existing lending facilities with more resources to cope with additional demand during times of crisis;
    - existing instruments to cope better with market volatility, including local currency borrowing and risk-mitigating hedging instruments;
11. review and expand as needed borrowing limits for developing countries while considering their debt sustainability as well as macro and debt management capacity;
12. continue to develop flexible instruments designed to support specific development budget financing as contingency arrangements during times of market disruption for countries with sound policies;
13. review the obstacles to an expansion of sub-sovereign lending and guarantees for credit enhancement, supported by a suitable national framework, and provided that local administrative capacities are sufficiently developed;
14. promote the resumption of international trade through emergency support to trade financing. In doing so, MDBs could increase time-bound guarantees, direct financing of infrastructure for trade and capacity building to trade facilitation. They could share views on their respective risk assessment policies and coordinate their initiatives. They should engage broader coordinated dialogue with other financial institutions, including export credit agencies (ECAs), to agree on principles to further increase the commercial sectors access to trade finance;
15. explore the merits of extending guarantees for credit enhancement of government issuances on the market.

For their part, G-20 members:

16. will partner with MDBs in providing short-term financing and risk-sharing. Such partnerships could involve participating in liquidity or credit facilities, such as the Liquidity Program for Growth Sustainability at the Inter-American Development Bank (IADB) and similar instruments of other MDBs.

B2. Regarding support for poor countries:

17. mindful of the impact that reduced ODA flows would have on the achievement of the Millennium Development Goals, G-20 members reaffirm the importance of the development assistance commitments they have made, and urge both developed and emerging economies to undertake commitments consistent with their capacities and roles in the global economy, which will increase ODA above the pre-crisis level.
18. G-20 members reaffirm that they will meet their commitments to the concessional arms of the MDBs. The G-20 emphasize the need for

countries that have made commitments to finance Multilateral Debt Relief Initiative (MDRI) to fulfill them.

The World Bank and the IMF:

19. should review the application of the Debt Sustainability Framework (DSF) with the view to make full use of its existing flexibility to reflect the diversity of situations across low-income countries. This should contribute to better leverage resources and to facilitate lending for investments with high economic returns without endangering the financial sustainability of the institutions. Lending should also be aligned with national strategies to ensure full country ownership.

MDBs should promptly:

20. assess the feasibility to increase concessional financing to the poorest countries as it is crucial in order to avoid setbacks in achieving MDGs due to the financial crisis;

21. ensure an effective response by exercising flexibility within country strategies and program and instrument choice. The response should be based on countries specific characteristics and needs, and enhanced through strengthening knowledge sharing, including through south-south cooperation, and conditionality appropriate to the crisis;

22. support sound and effective budgetary policies in low-income countries to help protect development expenditures in key areas such as health, education, nutrition and safety nets;

23. develop new tools — or customize existing ones — to facilitate sovereign risk management and access to markets, such as catastrophic risk insurance and local currency issuance.

For their part, G-20 members:

24. will partner the MDBs to protect the poorest people through the crisis, and provide additional resources for this purpose, for instance through increasing contributions to concessional funds or new facilities.

B3. Regarding support to the private sector, MDBs should selectively increase their activity on the basis of their comparative advantages, within the context of their risk management framework and clear long term strategies, including by:

25. evaluating guarantee facilities to make them more effective in leveraging other means of finance, and fully transparent to markets. This could also step-up efforts to develop bond-insurance schemes for creditworthy corporate actors;

26. better using balance sheets to meet infrastructure needs, in particular promoting private investment, and make readily available bridge financing, such as the IFC's infrastructure crisis facility, not only on a significantly bigger scale but also to bridge the financing gap for public infrastructure projects;

27. supporting financial institutions by reinforcing their capital basis where appropriate;

28. assisting investors from developed and emerging economies willing to invest in poorer countries during difficult times. MDBs also need to step up their outreach efforts towards private investors by better informing them about the situation in developing countries and providing enhanced risk mitigation solutions;

29. calling on the private sector arms of MDBs to play an important direct and catalytic role, including through syndicated ("B-loan") instruments, in light of the large refinancing requirement of developing economies, emerging market corporates, and the need to help institutions access finance. This includes trade finance and promoting the recapitalization of viable financial institutions;

30. reaffirming their commitments to meet targets for funding in low income countries and "frontier markets" to ensure that the overall portfolio of private sector operations remain balanced;

31. strengthening support for financial sector development in the formulation and implementation of financial regulations, in particular where private financial markets are not functioning properly, with a view to support long term development.

C. Resources and Capital Adequacy

32. G-20 countries will work with the MDBs to increase the Banks' financing (above usual financing commitments) by $US100 billion over 2009, 2010 and 2011 based on currently agreed capital. Furthermore, countries will continue working with the MDBs to see if there are other ways to more comprehensively utilize their balance sheets in responding to the crisis.

33. G-20 countries, through their involvement in the Boards of Governors, commit to urgently review the adequacy of the capital resources of all MDBs to provide appropriate increases in funding to mitigate the consequences of the crisis. Any increases should maintain appropriate safeguards and development effectiveness, and entail commitments to on-going governance reform.

34. The Asian Development Bank (ADB) should immediately proceed with a substantial general capital increase of 200%, or $US100 billion, to enable a sustainable level of lending in conjunction with the adoption of strong safeguards and governance reform. This decision requires a strengthening of the Bank's operational and risk management capacities.

35. The European Bank for Reconstruction and Development (EBRD) should promptly review its statutory capital constraints to give leeway to interventions by the Bank, while preserving its financial strength.

36. The G-20 countries through their representatives at the Executive Board of the African Development Bank (AfDB) stand ready to initiate a review process of the Bank's capital adequacy in May 2009, based on a review

of the Bank's operational limits and demand for basic development investment, and support for trade, the private sector, and the poorest.

37. The G-20 countries through their representatives at the Executive Board of the IADB are committed to initiate a review process of the adequacy of the Bank's capital by March 2009, alongside a review of the Bank's operational limits and demand for basic development investment, and support for trade, the private sector, and the poorest. G-20 countries stand ready to consider such a process for the Inter-American Investment Corporation.

38. The Islamic Development Bank (IsDB) currently has a reasonable level of resources to support appropriate lending growth. The IsDB should continue to keep its resource needs under review in light of the evolving situation in its member countries.

39. While the WBG is well capitalized and has sufficient resources for an initial response to the crisis, it should continue to make full use of its balance sheet and review its capital adequacy in the context of the deepening crisis, with special attention to the capital needs of the IFC to expand support for private sector recovery and the adequacy of concessional resources of IDA countries.

40. MDBs should make a concerted effort to design a common understanding of prudential ratios and capital adequacy, thereby enhancing transparency and comparability of their financial reporting, though this should not delay any required capital increase.

D. Governance Reform

MDBs should:

41. strengthen accountability of their management, and improving the processes to assess their performance. There is broad support from G-20 members for open, transparent, competitive, and merit-based selection process, irrespective of nationality and geographical preferences for the appointment of the senior management of the MDBs;

42. increase, in an open, transparent, competitive, and merit-based process, the proportion of employees, in particular senior management, from developing countries when they are under-represented in order to strengthen their country-based model, reinforce ownership on development strategies, and improve proximity to clients, including by delegating authorities to local offices.

The World Bank should:

43. accelerate reform of the voting power to reflect changing economic weights and systemic importance in the world economy, leading to a greater role of developing and emerging markets, while taking account of the uniqueness of MDBs' development mission, including contributions to concessional windows and the need to foster partnership within the development process.

G-20 members:

44. commit to ratify and implement promptly the first step of the Voice and Representation reform agreed to by the Governors during the 2008 World Bank Annual Meetings;

45. call for the Development Committee at its 2009 Spring Meeting to launch a wider discussion on improving governance and effectiveness of the World Bank, and to set an accelerated timeline for the second step of Voice and Representation reform package, with the aim to reach an agreement at the 2010 Spring Meeting.

    Within that process, members should consider the evolving weight of all members in the world economy and other Bank specific criteria consistent with the WBG's development mandate, moving over time towards equitable voting power between developed and developing members. Some members call for this enhancement of voting power to be achieved without dilution of any individual developing members.