

What's the World Bank Good For?

Ravi Kanbur

www.kanbur.dyson.cornell.edu

Lee Kuan Yew School of Public Policy, Singapore

20 October, 2017

Outline

- Introduction
- World Bank—From Origins to Present
- Global Public Goods: Theory and Division of Labor
- World Bank Specifics
- Conclusion

Introduction

- It should be clear to even a casual observer that all is not well with the World Bank.
- Staff morale is low. Discourse on “Mission creep” co-exists with “Lack of Mission”.
- Shareholders do not seem to be in love with the institution either.
- Using the indicator of the (lack of) success of the last capital increase, compared to the relative success of the Regional Development Banks and the IMF, and the propensity of subsets of shareholders to set up new multilateral development banks (MDBs), the shareholders of the World Bank do not seem to be putting their money where their mouths are, even when they mouth support for the institution.

Introduction

- As we shall see, this was not always so.
- The World Bank was a prized institution, credited with its share of glory for the post second world war recovery.
- Even when it was criticized and reviled by civil society in the years of structural adjustment and the Washington consensus, at least it demonstrated its relevance.
- The risk now is growing irrelevance as its financial base recedes relative to financial needs of countries on the one hand, and alternative supplies of finance on the other.

Introduction

- So much for the World Bank.
- Coming to the World, there is now a growing understanding, to the point of a crescendo of recognition, of the problems of cross-border spillovers and externalities, and of the inadequacy of global instruments to address these problems.
- Obviously, the problems include financial contagion, infectious diseases, climate change and migration.
- Our world of nation states is struggling to address these problems, for the equally obvious reason that there are insufficient incentives for any single country to invest in the solution, which must necessarily be cross-national.
- Mechanisms to address these cross-border issues are “Global Public Goods”.

Introduction

- We thus have a global institution which is falling into difficulties and irrelevance; and a set of problems which need a global institution to address them, to supply the Global Public Goods.
- Could there be a match? And what would need to happen for the match to be made and for it to succeed?
- These are the questions which I try to begin answering in this presentation.
- Although my motivating focus is on a single institution, The World Bank, and its potential role in addressing the problem of Global Public Goods, I hope that the issues raised will be general enough to merit broad discussion.

World Bank—From Origins to Present

- John Maynard Keynes, *Economic Consequences of the Peace*, 1919:
- “..the spokesmen of the French and British peoples have run the risk of completing the ruin which Germany began, by a peace which, if it is carried into effect, must impair yet further, when it might have restored, the delicate, complicated organization, already shaken and broken by war, through which European peoples can employ themselves and live.”
- “if the European war is to end with France and Italy abusing their momentary victorious power to destroy Germany and Austria-Hungary now prostrate, they invite their own destruction also...”

World Bank—From Origins to Present

- Opening remarks of John Maynard Keynes, as Chair of “Commission II” on the Bank for Reconstruction and Development,” 3 July, 1944.
- “...it will be authorised in proper cases and with due prudence to make loans to the countries of the world which have suffered from devastation of war, to enable them to restore their shattered economies and replace the instruments of production which have been lost or destroyed.”
- “...as soon as possible, and with increasing emphasis as time goes on, there is a second primary duty laid upon it, to develop the resources and productive capacity of the world, with special attention to the less developed countries....”

World Bank—From Origins to Present

- “Herein lies the novelty of the proposals which will be submitted to you....The proposal is....that all the member countries should share the risk in proportions which correspond to their capacity. The guarantees will be joint and several, up to the limit of any members’ subscription.”
- “...I fancy that the underlying conception of a joint and several guarantee of all the member countries throughout the world, in virtue of which they share the risks of projects of common interest and advantage even when they cannot themselves provide the lump sum loan originally required, thus separating the carrying of risk from the provision of funds, may be a contribution of fundamental value and importance”

World Bank—From Origins to Present

- This design of John Maynard Keynes and Harry Dexter White (who led the US delegation) succeeded brilliantly. Financial intermediation between sources of funds and uses of funds was successful, and contributed to the rapid post-war recovery and growth.
- After the first phase, the model was modified to include concessional funding as the newly independent developing economies came on the scene.
- The model was also replicated through the Regional Development Banks and sub-Regional Development Banks. The reasons for this proliferation of the model, which continues to this day through AIIB and NDB, are perhaps mainly political, but the proliferation is testament to the power of the model.

World Bank—From Origins to Present

- But notice that in the original conception the use of funds is basically for country level investment. There is no mention of the modern cross-border issues of climate change, infectious disease control, migration, or financial contagion as being part of the remit of the World Bank.
- These are of course the issues of our time. But, in keeping with the original model, despite a ramping up of rhetoric from all multilateral development banks on cross-border spillover and public goods, the overwhelming focus is still on country by country investment.

World Bank—From Origins to Present

- But, as a curiosum perhaps, note that despite the fact that are not mentioned explicitly, GPGs do make an appearance in the original Bretton Woods discourse in at least two senses.
- First, the very general sense that recovery of war torn economies is in the interests of the world as a whole—a very different perspective than the one taken in the Treaty of Versailles.
- Second, the cooperative design of funding, the “joint and several guarantee” mechanism, is itself a Global Public Good. It addresses insufficient incentives on the part of any one country to bear the risks of investment to rebuild infrastructure destroyed by the war.

World Bank—From Origins to Present

- Let us turn then to some conceptual foundations for how an agency like the World Bank might interact with GPG issues.

Global Public Goods: Theory and Division of Labour

- There are many externalities and spillovers across sovereign nation states.
- Four obvious ones mentioned earlier are financial contagion, infectious diseases, climate change and migration.
- But another important aspect of these spillovers is their reach and spread.
- Many are restricted to a contained number of contiguous nation states. For example, riparian rights across countries sharing river basins and water tables, or when forest cover or wildlife movements stretch across borders, or when conflict in one country leads to refugee flows only to a neighboring country.

Global Public Goods: Theory and Division of Labour

- There are conflicting tradeoffs in designing mechanisms and institutions to address these externalities. And it is these mechanisms and institutions which are the public goods.
- The principle of subsidiarity says that all other things equal, and if the setting up of mechanisms were costless, the mechanism addressing a problem should be located closest to where that problem is.
- Thus the principle would resist an immediate jump to a global institution to address multi-country issues in Africa, or in Latin America, or in Asia.

Global Public Goods: Theory and Division of Labour

- But, of course, mechanisms and institutions are not costless. There are large fixed costs of setting up institutions, which suggests a small number of institutions. But how many and of what type?
- A detailed cost-benefit would be difficult if not impossible to conduct, but suggests a split between Regional Institutions for within-region spillovers and Global Institutions for spillovers which are global in the sense that they encompass countries from across regions.
- There is no reason why a three-country riparian rights issue in Asia, for example, should necessarily be handled by a global institution like the World Bank if there is a regional institution capable of handling it.

Global Public Goods: Theory and Division of Labour

- If the subsidiarity argument has validity, then regional Public Goods (RPGs) should be handled by Regional Institutions, and GPGs by Global Institutions.
- Thus for a Global Institution like the World Bank, the rationale for involvement in cross-border externalities cannot simply be that they exist, but that they are Global and cross-regional in nature.

Global Public Goods: Theory and Division of Labour

- There is yet another type of question on the division of labor. For truly global issues, should there be a global institution per issue, or should there be a global institution handling multiple issues?
- There is a tension or tradeoff between issue focus and design of the mechanism at the global level (which is the GPG), for example for infectious diseases, and implementation of the mechanism at the country level. A smooth translation from one to the other is necessary, and this may be best achieved by having both under one roof, but the trade off has to be recognized.

Global Public Goods: Theory and Division of Labour

- Let us turn now to a fundamental point about the trade offs in use of resources of the development banks, the World Bank in particular. Should they be used for development and poverty reduction on a country by country basis, or should they be used for provision of GPGs?
- Of course one could avoid the question by saying that GPGs address development and poverty reduction as well. But this does not face up the tradeoff that the marginal dollar could be spent on building schools or health posts versus developing clean energy devices to reduce fossil fuel usage.

Global Public Goods: Theory and Division of Labour

- This is not an easy question to answer definitively and quantitatively.
- But it can be argued that up to now resources of the development banks have only been minimally devoted to GPGs.
- There should be a shift towards (i) financing the setting up of global mechanisms to address GPGs and (ii) financing the country specific investments required by the global mechanism.
- However, Ray Offenheiser provides an alternative perspective in a dissenting note to the recent Center for Global Development report on Multilateral Development Banks:

Global Public Goods: Theory and Division of Labour

- “What separates the MDBs in this fast-changing context, however, is their specific mandate to reduce poverty.....While I would certainly recognize the role of global public goods (GPGs) in addressing different dimensions of poverty and inequality....and perhaps even recommend making it an explicit and major pillar of work, I would continue to argue that the overarching mission and mandate of the World Bank (and other MDBs) must remain the fight to eliminate extreme poverty.”
- This is surely a different voice on the division of labor between financing for GPGs and financing for country specific investments for poverty reduction.

Global Public Goods: Theory and Division of Labour

- However, the financing issue immediately brings up another fundamental question—the suitability of the development banks' signature instrument, the sovereign loan, for financing GPG mechanisms.
- Since the whole point about GPGs is the difficulty of attributing country specific costs and benefits, the sovereign loan instrument is peculiarly unsuited to the task. Various related mechanisms (eg Apex lending) have been tried, but the fundamental issue remains unchanged.

Global Public Goods: Theory and Division of Labour

- The answer has to be that the core financial instrument for GPGs has to be a grant instrument.
- This is recognized in a recent Center for Global Development Report which proposes a new grant financing window for the World Bank alone of \$10b annually. It raises the question then of whether similar windows should also be opened for the regional development banks.
- And it is the use of grant resources in this manner, rather than for direct poverty reduction, which Ray Offenheiser is dissenting from.

World Bank Specifics

- So, what is the World Bank good for?
- As an institution for country specific investment for development and poverty reduction, the world community has revealed a preference for other institutions—regional development banks, new development banks, and other multilateral and bilateral vehicles.
- It is not clear if this trend can be reversed.

World Bank Specifics

- There appears to be more global support for a generic GPG argument for financing. But:
 - For region specific cross-country public goods, regional institutions are superior in principle.
 - For genuinely global GPGs, there is the question of whether the world community should primarily go for issue specific global institutions.
 - The sovereign loan instrument is not suitable for GPGs, and there are strong tradeoffs in use of grant resources for GPGs rather than country specific poverty reduction.

World Bank Specifics

- However, there are strong arguments for using the World Bank to advance the GPG agenda:
 - It is indeed a global institution, with a global mandate and an as yet inadequate but potentially reformable global governance structure.
 - Its country specific operations give it a platform to implement the country level actions needed in a global mechanism.
 - It has experience of and is trusted in, managing trust funds for grant funding.
- If the international community wished to , it could build on these strengths and develop a GPG mandate for the World Bank, as argued in the Center for Global Development Report.

World Bank Specifics

- Beyond the standard GPGs there is, in particular, one GPG for which the international community already relies on the World Bank, and which the World Bank could do more of.
- GPGs are contentious issues and it is not easy to arrive at a global consensus on the way forward, in general and in specifics. And without a consensus there is no way forward—that is almost definitional for a GPG.
- But the development of global consensus is itself a GPG. Thus consensus on GPGs has all the issues of underinvestment faced by other GPGs. No single party has the full incentive to achieve consensus, because the costs are party specific but the benefits are dispersed.

World Bank Specifics

- The international community needs institutions which help to develop global consensus, and to maintain it. The role of globally acceptable data and analysis is crucial.
- For example, SDG 1.1 is to eliminate extreme poverty. But who is to define extreme poverty? Who is to collect, collate and manage the data to monitor this global goal? Who is to develop and maintain global consensus on these seemingly technical but often starkly political questions?
- The recent report of the Atkinson Commission on measurement of global poverty, commissioned by the World Bank, is an example of a consensus building exercise which can help the global community come together around SDG 1.1 and other SDGs. It is a significant contribution to an underappreciated GPG.

World Bank Specifics

- Consensus building of this type has two prerequisites—technical excellence and actual and perceived independence. Both of these were satisfied in the case of the Atkinson Commission.
- But the governance structure of the World Bank mitigates against perceived and perhaps actual independence of consensus building exercises. These structures have to move to reflect the economic realities of mid 21st century, rather than the realities of the mid-20th century.
- And, of course, such activities require grant resources.

Conclusion

- The World Bank is in the doldrums, or worse.
- The GPG argument is often put forward as a way of reviving and even rescuing the institution.
- But the argument needs to be unpacked and examined critically.
 - First, GPG has to be genuinely global, not just regional, for a global institution to be given the lead in addressing the issue.
 - Second, there may be an argument for issue specific global institutions, for example for infectious diseases.
 - Third, the central instrument of the World Bank, the sovereign country loan, is unsuited to financing of GPGs.

Conclusion

- However, the World Bank does have certain advantages, including
 - Technical excellence and convening power to help build consensus on a range of GPG issues, although this needs to be enhanced by reform of its governance structures.
 - Experience with managing concessional and grant resources which will be central to financing GPGs mechanisms.
 - Experience with country operations to implement the country specific dimensions of GPG mechanisms.
- Thus, a combination of (i) continued country specific operations of the conventional type but a relative expansion of (ii) focus on consensus building on and design of GPG mechanisms and (iii) their implementation at the country level seems to be the road to viability for the World Bank. But for this the governance structures will have to be reformed to reflect the economic weights not of 1944 but of 2019, 75 years after Bretton Woods.
- That's what the World Bank is good for now, three quarters of a century after its founding.

Thank You!