POLICY MEMO

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The need for a much bigger World Bank Group, focused on the Twin Goals

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This non-paper makes the case for a significant capital increase in the context of resources being allocated to countries where the need is greatest, while maintaining a strong offer across the spectrum of World Bank clients, and ensuring appropriate risk management and financial sustainability.

1. Decisions on the future of the World Bank Group (WBG) through the "Forward Look" process and design of the new IDA financing framework provide a critical opportunity to set out a coherent vision for how the WBG can be fit for purpose through to 2030. Integral to this vision – and whether it will lead to a historic shift through which the WBG will be able to deliver its Twin Goals – are decisions on how ambitious we should be about the size of IDA and IBRD and how resources should best be allocated.

2. A substantial increase in financial resources, directed where they are needed, is necessary to achieve our collective political commitments to the Sustainable Development Goals (SDGs) and to the Paris climate change agreement. We will only get to the trillions of dollars through a combination of private and public resources, both domestic and international. We need to be ambitious on all four fronts and, as agreed in Addis Ababa, to step up our efforts to achieve this.

3. A strong network of international financial institutions (IFIs), led by a more effective and more relevant WBG, will be central to our success. IFIs' ability to leverage limited international public funds makes them the most important part of the international development finance system when resources are scarce. The WBG has a unique role within the IFIs, given its ability to provide finance and share knowledge across all regions, and bring countries together around global issues. However, the current size of the WBG, and the way in which it allocates resources are not well matched to its objectives of the Twin Goals, and therefore its contribution to achieving the SDGs and climate commitments.

4. In terms of size, in real terms IBRD is now only lending the same as it did 30 years ago, whilst the Word Bank as a whole committed only 50% as much in 2015 in real terms as it did in 1985. At the same time, the growth of the economies to which IBRD lends has meant that the relative significance of the World Bank has shrunk, reducing its ability to make a difference to poverty reduction and economic development. Alongside its experience and knowledge, the WBG needs financial firepower, if it is to make a difference in a large number of its clients. We need to raise the level of our ambition. As highlighted in the Forward Look papers, in order to maintain the long-term average IBRD lending capacity of $27bn, there is an equity gap of around $12bn. Raising our ambition to annual lending capacity of $40bn and beyond to $50bn, the gap increases to at least $26bn and $36bn, respectively.

5. As international public resources, especially scare concessional resources, will always be less than we ideally need, it is even more important that we allocate them as effectively as possible for achieving the SDGs and the Twin Goals. It will not make sense to increase the size of IDA or IBRD if resources are not directed to where they are needed most (or, indeed, delivered in a faster, more responsive, agile way).

6. As we noted in Addis Ababa, it is important that we focus our resources on those with the greatest needs and least ability to mobilise other resources. The current pattern of allocation of IDA does this relatively well, although allocation to the very poorest is being improved and retaining the use of IDA for those below the graduation threshold is important. The current pattern of allocation of IBRD resources does not do this. Only half of IBRD commitments currently go to the lower MICs with a greater need to borrow higher volumes of IFI finance, whilst the other half go to countries which are technically above the IBRD graduation threshold, and have higher access to their own and market finance. Commitments in FY2015 showed that HICs got $33 per capita, compared to LMICs which got $4 per capita, eight times less. UMICs got 25% more than LMICs. The current offer from the IBRD for graduates from IDA is only $6 per capita despite their higher levels of poverty and lower ability to self-finance poverty reduction.

7. The chart below shows the stacked commitments that a sample set of IDA and IBRD countries have received for the period 2011-2015. In principle, you might want to see a trend line moving from top left to bottom right i.e. the richer the country (per capita), the lower the World Bank finance (per capita). However, there is no apparent link in IBRD. With the exception of Rwanda, no IDA eligible country received over $75 per capita. For IBRD recipients, six LMICs, five UMICs and two HICs received over this amount.

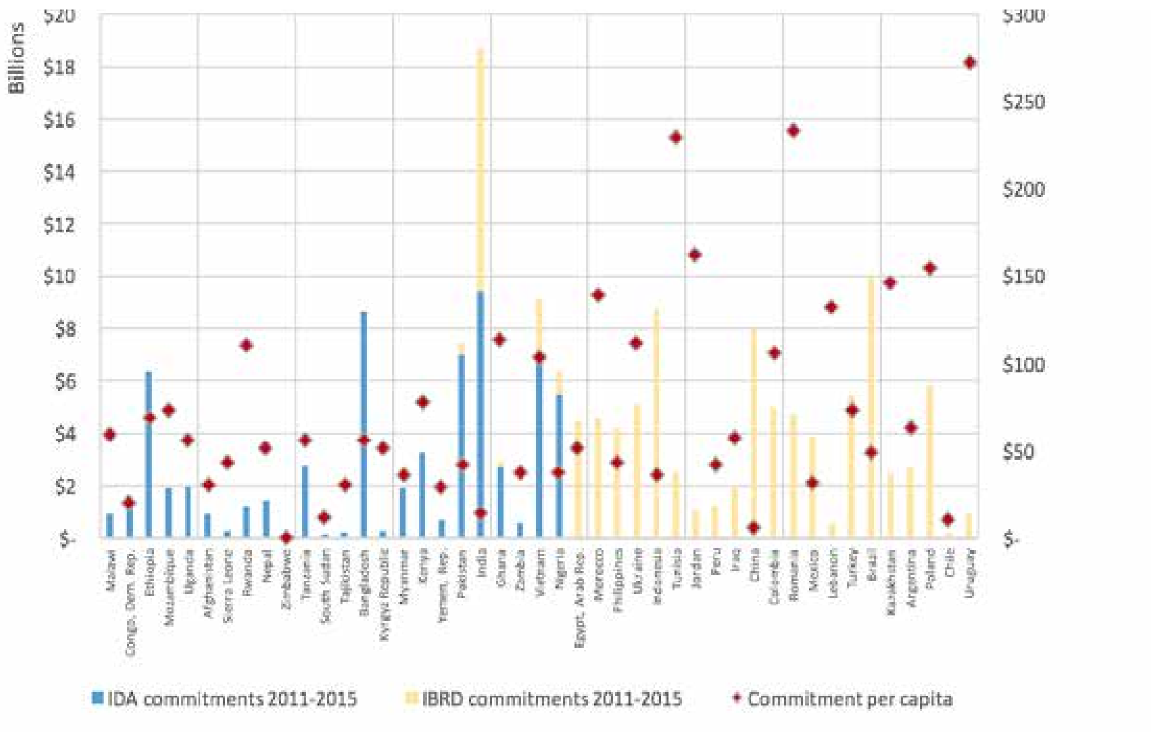


Chart 1 – Historical IDA and IBRD commitments, by volume and in per capita terms. Volume is on the left hand axis, with the stacked bars, showing the total amount. The axis on the right hand side, with the floating diamonds, shows how much this translates to per capita spend. Countries are ordered left-to-right in terms of increasing GNI per capita.

We therefore propose the following principles be considered for the allocation of WBG resources:

- The WBG must remain **financially sustainable** and be able to **manage risk** in a way consistent with retaining its AAA rating (both in IBRD and, once leveraged, IDA).
- The Bank should continue to **serve all its clients** with knowledge, finance and a range of financial instruments. The combination of these should reflect the WBG's objectives, and the needs and income level of the client. Staff should be incentivized for providing the right offer to the right country.
- Financial volumes from the WBG should be aligned with the WBG's strategic objectives. In doing so, financial volumes should be prioritized for those countries with **highest levels of poverty and limited ability to finance their own poverty reduction** through domestic resources or access to market finance.
- Given that demand from the **poorest and most fragile** will stay strong in the medium to long term, the WBG needs to be able to work at scale in the most fragile countries and on the most intractable issues. We should be ambitious to meet that demand.
- Concerns about **absorptive capacity** should, as far as possible, be addressed through programming which builds capacity over time and use of instruments, delivery mechanisms and risk mitigation which match the context. This should limit the extent to which resources which are needed (from a poverty and ability to self-finance point of view) are reduced.
- **IDA's balance sheet** should be used first and foremost for the **poorest countries**, reflecting the basis on which IDA funds have been provided since 1960.
- **IBRD's balance sheet** should be used for those with an **ability** (debt-carrying capacity) **to borrow** at IBRD rates.
- Price should take account of a country's debt sustainability and ability to pay. This is reflected in the current spectrum of grant, IDA-only, blend and IBRD. **Further differential pricing** in IBRD should be introduced.
- **Transfers** between different parts of the WBG allow for better achievement of the WBG's Twin Goals and sustainability of the balance sheets, seen together.

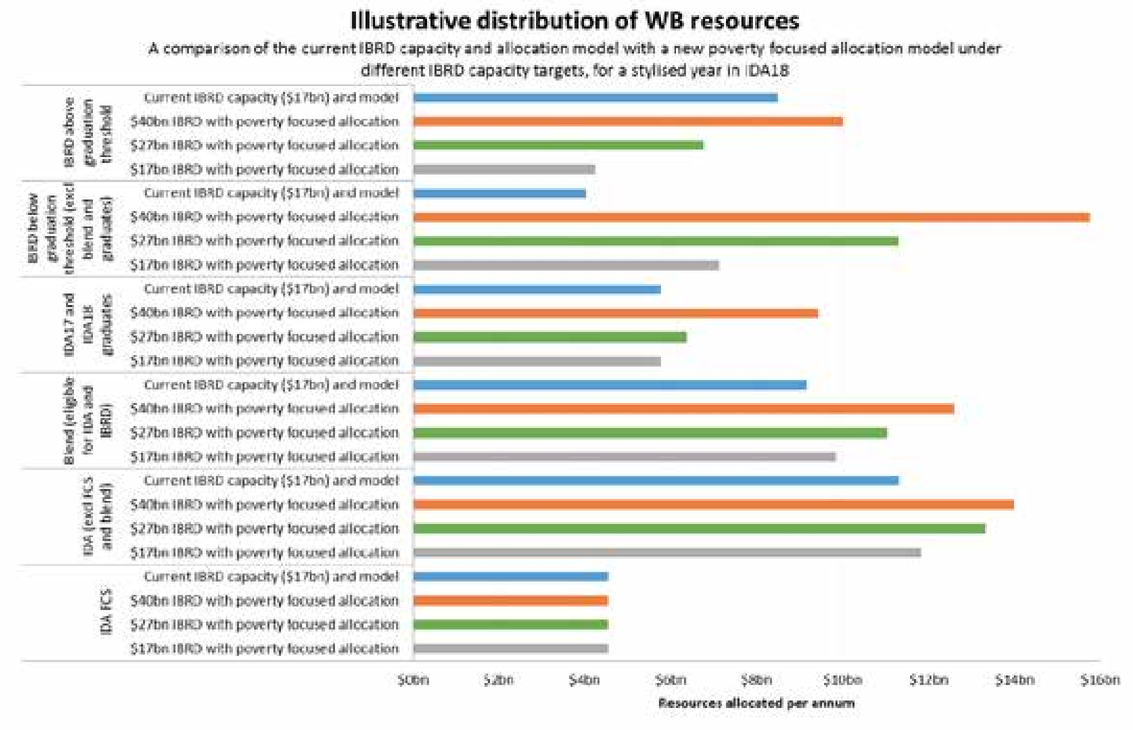
For IDA, we propose consideration of the following principles:

- We should be **ambitious about overall resourcing**, including net income transfers to IDA and a high ambition for IDA leverage, particularly at the outset of IDA18.
- **Concessional IDA resources** are valuable and scarce so should be focused on countries with greatest needs now and in the future. Such resources should continue to be allocated through a **performance-based formula**, with a stronger focus on need and adjustments to increase resources for FCAS, as proposed.
- **Non-concessional IDA resources** should also be used first and foremost to the benefit of the poorest countries, reducing their reliance on costly market finance.
- Given the need to preserve concessional and non-concessional IDA resources for the poorest countries, **IDA should not support countries once they have graduated** (see IBRD section below for more on graduates). The blend period should be used more actively to help countries transition from IDA to IBRD.

For IBRD, we propose consideration of the following principles

- We should be **ambitious on the future size of IBRD**, with capital measures commensurate with this. This equity gap could be closed through a combination of capital measures, including SCI, GCI, price, expenditure and income measures, and balance sheet optimisation.
- IBRD should continue to **serve and be relevant to its full range of clients**.
- The Board should discuss and **agree expected lending volumes** for IBRD each year.
- A proxy for **poverty and ability to self-finance your own poverty reduction**, such as GNI per capita, should serve as the **benchmark for the allocation of financing**, with greater allocations per capita for poorer countries with least ability to self-finance. We would like to work towards a ratio of 1:3 in terms of volume of loans going to countries above and below the IBRD graduation threshold.
- Flexibility should be retained. There **should neither be a binding allocation formula nor formal Board approval of country allocations**. There should be an iterative process with clients and finance should supporting results in line with priorities identified in **SCDs and CPFs**. Second-order factors could be added such as the need for **crisis finance** (complementary to the IMF and based on risk-financing approach, as far as possible) or to tackle **climate change**. The basis for layering these additional factors on top of the primary GNI/capita-based allocation process should be as transparent as possible.
- **IBRD should finance IDA graduates**. A GNI/capita model would provide resources commensurate with the needs of graduates. In doing so, it should only take account of past allocations in so far as to avoid any major unplanned fiscal shock. IDA resources should only ever be considered when all options for IBRD support have been exhausted.
- **IBRD should be available in greater volumes than it is currently to 'IDA-only' and 'blend' countries**, commensurate with their level of poverty and ability to self-finance poverty reduction, but limited by their debt carrying capacity.

The chart below shows a stylised set of allocations for an imagined year into the future, using the IDA18 High 1 Scenario for IDA and different scenarios for IBRD lending capacity.



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