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ADDRESS BY THE GOVERNOR FOR SWITZERLAND
AT THE THIRD PLENARY SESSION

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1. On behalf of Switzerland, I would like to extend my gratitude to the Brazilian authorities for their excellent and generous arrangements and their warm welcome in this beautiful country.

The Region

2. Latin America has faced a difficult year in 2001 and the outlook for the next year is mixed. The recent signs of improvement of the global economy and in particular in the United States make us hopeful that a recovery is possible in the next year at least for those countries with sound fundamentals – and these are not few.

3. The situation is more protracted in Argentina, and the recent capital flight in Venezuela demonstrates that international investors still remain sensitive to political instability and the associated insecurity about a country's economic policy. This should also be a sign for those countries where elections are impending.

4. Access to capital markets will remain constrained and recourse to external finance will also be limited by relatively high fiscal deficits. In this situation private sector lending for long-term investment becomes particularly important. The countries of the Region will have to make a particular effort to regain the trust of private investors and to attract financial flows that will not burden their households. For this, economic policy makers must pursue more decisively the improvement of the institutional and legal frameworks and the general business environments in their countries, and renew their commitment to trade liberalization.

5. After Doha, I am hopeful that the integration efforts of the Region will regain momentum. Cooperation within Mercosur as well as between Mercosur and the EU or the FTAA should be renewed. Regional integration is particularly important for Latin America and the Caribbean. For one, it benefits also smaller and medium-sized companies and thus will most likely have a greater impact on employment generation and poverty reduction. But it also provides the countries of the Region with a stronger negotiating position vis-à-vis their

trading partners in the North. Thus, I also encourage to accelerate integration efforts in Central America and the Andean countries. Moving forward from Doha, all participants, be it in the North or in the South, must demonstrate a greater commitment to the framework and procedures laid out by the WTO. The importance of this point has been underlined yet again by the recent trade dispute on steel.

6. Productivity gaps between the Region and the industrialized countries, as well as within the Region, are on the rise. Latin America and the Caribbean must still find its way towards more inclusive and equitable growth. In support of this process, the Bank must promote institutional and legal reform, the development of small and medium-sized business as well as affordable and universal access to social services, including health, basic education and vocational training. While infrastructure remains an important goal of the Bank, its operations need to place greater emphasis on productivity, opportunity and social development. It is against this background that we will have to discuss the new lending framework, the demand for new instruments and the Bank's role in private sector development.

Argentina

7. I am deeply concerned about the situation in Argentina. While a solution to the crisis is primarily in the hands of the Government, the international community needs to stay engaged and stand ready to support Argentina if necessary and feasible. The Bank can play a key role in mobilizing international know-how and advice from within and outside the Region as well as financial support for a viable economic stabilization package.

8. We also need to learn from the case of Argentina. What has triggered the collapse of the Argentinean economy and what role can the Bank play to avoid that such a scenario reoccurs in the Region? What are the policy implications for other countries in Latin America and the Caribbean with a fixed exchange rate or dollarized economy? And what can Argentina learn from its neighbors that initially followed the same course, but eventually took a different approach? I encourage the Bank to analyze these issues carefully and to prepare a corresponding Report for Governors that we can discuss next year. Evidently, any attempt to look into the past must also take into account the important achievements of Argentina over the past decade in terms of modernizing its economy.

Development Effectiveness

9. Public institutions throughout the world are increasingly scrutinized for effectiveness and are asked to demonstrate the results of their actions. The international financial institutions are not exempt from the quest for greater accountability for the development impact they achieve (or do not achieve) in cooperation with borrowers. I welcome the current, intensified debate about development effectiveness and what it necessarily implies: greater emphasis on outcomes and impact in lieu of inputs and outputs, better measurability in favor of professional and systematic evaluation, and - last but not least - a change of the corporate culture and incentive framework in many international institutions, including the IDB.

10. Evaluation is an indispensable aspect of results-based public management. It is to the public sector what accounting and auditing are to the private sector. It can play an important

role in guiding the selectivity for which we must strive in the pursuit of results on the ground. The Bank's shareholders have recognized this when, some two years ago, they redefined, reorganized and strengthened the evaluation function in the Bank, creating the independent Office of Evaluation and Oversight. The Office is delivering on an ambitious work program. I hope that the debate engendered by the products of the Office begins to be reflected in the design of Bank programs and projects. Both programs and projects should increasingly include explicit results frameworks in order to facilitate evaluation and thus accountability. The IDB has made major strides forward in putting the issue of development effectiveness on the table. I think the Bank is on the right track in this regard, Mr. President, and I would like to congratulate you and your colleagues on this achievement.

11. The Report on Development Effectiveness submitted to Governors contains some important recommendations to Management. In particular, the Bank should incorporate results-reporting in its annual portfolio review by the Regional Operations departments and create a separate Development Effectiveness Assessment Unit that would review independently all projects under preparation and report directly to the Executive Vice President. The mere creation of such a unit would not be sufficient to change the Bank's behavior. The operational units would also have to be willing to take on board any recommendations by such a unit, and this requires the endorsement by Senior Management.

A New Lending Framework and Proposed New Instruments

12. Switzerland supports the proposed measures to enhance the response capacity of the Inter-American Development Bank. The new lending framework represents a significant breakthrough in modernizing the Bank's lending approach and adapting it to the changed financing needs of the Region. The challenge will be to implement the framework by developing new and more flexible lending instruments that can be reconciled with the core mandate and financial integrity of the Bank and to put in place a system to strengthen IDB's development effectiveness in the region. These matters should be discussed by the Board of Executive Directors and not be referred to Governors.

13. At this stage, my only comment relates to the preferred creditor status of the Bank. This is not something that can be unilaterally proclaimed by the charter of any institution, but must be recognized de facto by a majority of the international community. Sovereign guarantees are a crucial ingredient for the preferred creditor status to be respected. IDB member countries have already made a major concession towards loosening the preferred creditor status when they raised the ceiling for private sector operations to 10 percent of the Bank's portfolio. It would therefore be irresponsible to further weaken the Bank's position by allowing the Bank to lend to sub-national entities without central government guarantees. This is not to say that the Bank should not expand its cooperation with sub-national entities.

Private Sector Development

14. The increase of the cap on private sector lending needs to be seen as part and parcel of the modernization of the Bank's instruments. The main issue here is additionality. We must not replace private capital, but mobilize it. IDB operations should pay greater attention to employment generation if we want to place private sector development at the service of equitable growth and poverty reduction. Risk management needs to be scaled up quickly and

a regular reporting system on the status of the private sector portfolio should be put in place. This is all the more important, given that a substantial portion of PRI's portfolio has come under pressure due to the economic deterioration in Latin America and the Caribbean.

15. Coordination between PRI, IIC and MIF has improved during the past year. Yet, there remains significant scope to increase cooperation at the strategic level. To create a new affiliate for private sector activities would be premature, however.

16. Mr. President, I am concerned about the performance of IIC, which has been adversely affected by the global economic downturn and the crisis in Argentina in particular. But in addition, IIC did not meet our expectations regarding business generation, which is lagging significantly behind the projections made during the General Capital Increase. This leaves IIC with a less diverse and more vulnerable portfolio. Management must rapidly develop a response plan to address the situation.

IDB and the Environment

17. In light of the upcoming Environmental Summit in Johannesburg, the review of the Bank's environmental activities is timely. The strategic work in this area should go beyond environmental management and also look at issues relating to sustainable development as well as prevention and management of natural disasters, such as earthquakes, flooding and desertification. In this connection, I encourage the Bank to further elaborate its specific role and comparative advantage vis-à-vis other multilateral organizations.

18. While IDB has made good progress towards the goals set out in the Institutional Strategy, lending for the environment and natural resources has decreased from US\$485 million in 1990 to US\$408 million in 1998. While structural causes may also have been in play, I call upon the Bank to reverse this trend and ensure that it will once again become a lead player in promoting environment and sustainable development in Latin America and the Caribbean. It would also be opportune to review the classification of environmental lending. A large-scale water and sanitation infrastructure rehabilitation project, for example, is a completely different story from an income generation project for indigenous people in the rain forest. This differentiation is necessary, if we want to be fully able to grasp the Bank's efforts in this field.

19. Whenever possible, the Bank needs to treat the environment issue in the broader context of poverty, and ensure that there is a clear link between environmental protection and poverty reduction. Last but not least, the Bank can make an important difference by more rigorously incorporating environmental aspects in its traditional work. Emphasis should be on indicators, harmonization of standards and procedures and enforcing EIA compliance. This needs to be supported by an incentive framework that encourages staff to take a pro-active attitude to environmental issues in their daily work.

Conclusion

20. The Bank has made significant progress at the strategic level to modernize and adapt its instruments to the new needs and requirements of the Region. The challenge will be implementation. The Bank needs to be flexible and pragmatic, and review progress after two years. Despite the shift towards more policy based lending it should not neglect its traditional

work. Social development and environmental management are key domains in which the Bank must maintain the lead and spearhead new initiatives that will lead to more inclusive and sustainable growth.