



COMMITTEE OF THE BOARD OF GOVERNORS
INTER-AMERICAN DEVELOPMENT BANK

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**REMARKS BY MR. ENRIQUE V. IGLESIAS,
PRESIDENT OF THE INTER-AMERICAN DEVELOPMENT BANK,
AT THE EIGHTY-SIXTH MEETING
OF THE COMMITTEE OF THE BOARD OF GOVERNORS**

Fortaleza, Brazil – 10 March 2002

Members of the Committee of the Board of Governors:

Resolution AG-5/01, adopted in March 2001 at the Forty-second Annual Meeting of the Board of Governors in Santiago, Chile, called upon the Committee of the Board of Governors to follow the discussions during the subsequent months on shareholders' needs and the role that the Bank should play in the new international financial architecture. The Committee was also called upon to consider proposals to increase the Bank's capacity to respond to new requirements in the countries, while preserving its financial soundness as well as its fundamental mission of promoting economic and social development and regional integration, and reducing poverty in Latin America and the Caribbean.

In response to the points raised during the Governors' discussions and the analysis presented by Management (document CA-425), a number of initiatives were launched during the year to help underpin and bolster the Bank's activity.

In 2001, the region—and, by extension, the Bank—stood at an important crossroads. Times of crisis are also often times of confusion. Highest priority must be given to interpreting the nature of the events and the direction in which the changes are heading—and, in the Bank's case, to a concerted effort by the institution's leadership. At a time when the paradigm underlying the Bank's decision-making processes is being called into question, we must rethink, if not the institution's core objectives, then at least the means to achieve them.

Given the Bank's central role in ensuring financial flows to its member countries and the supply of regional public goods, the way in which the organization is governed and managed should assure that its priorities reflect the needs of its member countries. This special relationship between the Bank and its borrowing members is what enables it to make a relevant contribution and impact upon key policy decisions in critical areas for social and economic development. This relationship takes two forms essentially: technical assistance, including policy dialogue, and financial services.

The challenge facing the Bank is simple: how to update itself in line with the changing needs and demands of its member countries, while reaffirming its origins and relevance and preserving its identity and financial soundness.

In 2001 we asked ourselves what the Bank needed in order to address new country realities and demands and what new instruments might help the Bank to act countercyclically in its member countries, enhancing the quality of its interventions and their contribution to the region's social and economic development.

During the year, the Governors and the Executive Directors examined the issue of how to make the Bank more responsive to the development needs of its member countries, seeking to make the best possible use of its resources without adversely affecting the allocation of these services among the various country groups.

At the same time, Management sought to identify and smooth out rigidities in the production of the Bank's services, and the Office of Evaluation and Oversight embarked upon a timely and productive work program.

The following are some of the highlights of key initiatives launched in 2001.

A. Highlights of the year 2001

1. New lending framework

Pursuant to the Santiago resolution, the Committee of the Board of Governors adopted a resolution presenting a new operating framework for the Bank. The proposal, which has already been approved by a majority of the Governors, sets the stage for "updating" the Bank in light of recent international economic and financial trends and their impact on national economies in the

region. This implies not just reaffirming the institution's mandates and updating its financing instruments, but also a more comprehensive view of the Bank's function. The proposal stems from a concern to ensure a presence that is at once timely, adequate, and, most importantly, effective; in other words, a presence that can help to attain the goals pursued by the Bank itself and contribute to the development objectives of the countries. The decision taken recently by the Governors clearly signals the need to update the lending framework, but also to assess its relevance in terms of each instrument's development effectiveness. For this, all Bank operations must have clear targets and objectives as well as appropriate benchmarks for measuring progress during implementation and for measuring final outcomes.

Once approved, the new operating framework—which would remain in place for a three-year period starting 1 January 2002—is expected to enhance the Bank's response capacity vis-à-vis its member countries in the region by means of the following financing instruments: (i) an investment lending facility in the amount of approximately US\$15.5 billion for the period 2002-2004; (ii) a policy-based lending facility authorized up to a ceiling of US\$4.5 billion drawn on the Ordinary Capital and US\$300 million drawn on the Fund for Special Operations (FSO); and (iii) a special US\$6 billion emergency financing facility under the Ordinary Capital (OC), to be executed during 2002-2003 and renewed for 2007-2008. During the exercise to reallocate available FSO resources among eligible countries, a reserve was established at the Board of Executive Directors' initiative to be used to finance emergency operations in OC-ineligible countries.

Each of these facilities will be implemented through financing instruments to be considered and approved by the Board of Executive Directors. To help borrowers expand their capacity to absorb resources to finance investment programs, Management will provide the necessary support by means of day-to-day monitoring of project execution and country dialogue as part of missions for programming and portfolio review; project identification, orientation and analysis; project start-up workshops; and technical-cooperation projects for institutional strengthening.

The size and composition of the lending program authorized for 2001 accurately reflected the impact that new patterns in world economic growth and international markets had had on the borrowing member countries; and this impact deepened over the months. Equipped with a limited set of instruments, and bearing in mind that the special financial emergency facility had

lapsed, the Bank had to remodel its available instruments in order to provide support to countries in crisis. In Santiago, we informed the Governors that demand for policy-based lending would likely remain high owing to the changes in the international setting (document CA-423), with pipeline estimates placing it in the neighborhood of US\$3.6 billion. In the wake of the crisis that swept the external sector, in 2001 the amount of US\$3,125 million was authorized in lending through financing instruments that were more in tune with country needs.

The decision to reopen the emergency lending facility as of 2002 represents an acknowledgement that, although the International Monetary Fund (IMF) holds central responsibility for heading up adjustment programs and programs for overcoming financial crises, the Bank's role is to proffer financial support to mitigate the impact of these crises on social and economic development, especially for society's most vulnerable groups.

But, investment projects continue to be the Bank's basic financial instrument, as set forth in the Agreement Establishing the Bank. Our activity in the area of policy-based lending serves to highlight the importance of working with our countries in designing the structural changes needed in order to move forward with processes of economic modernization and social efficiency.

The Bank's emergency loans are, by definition, exceptional measures and are subsidiary to agreements between countries and the IMF; they focus specifically on alleviating the social costs of adjustment and on sustaining reforms. Ever mindful of the fact that crises often trigger drastic setbacks in growth and development, the Bank has been sensitive to the special financing needs of countries grappling with severe economic difficulties or natural disasters. In this connection, we could point to the contributions made since 1977 as testimony of the Bank's collaboration in support of recovery programs for countries thrown into emergency situations.¹

As countries obtain broader access to private capital markets and build greater international trust and credibility, the demand for credit from the Bank will surely shrink as a logical and salutary outgrowth of the development process.

¹ See Special Operating Program for 1983-1984, including Annex I (document GN-1451-2).

2. Support for international negotiations

The past year has been encouraging for integration, trade, and open markets. Of special note was the launch of the World Trade Organization's Doha Development Agenda, given its comprehensive scope and special attention to the needs and interests of developing countries. China's entry into the WTO also clearly is a landmark event. The Free Trade Area of the Americas (FTAA) negotiations continue to advance, as do the European Union's negotiations with MERCOSUR. Work is proceeding apace on agendas for deepening the subregional agreements. In addition, the United States government's pursuit of trade promotion authority, coupled with its recent decision to pursue bilateral free trade initiatives in the Hemisphere, are positive signs of a commitment to freer world trade. We also have witnessed unprecedented regional cooperation initiatives in the launching of the Puebla-Panama Plan and the Initiative for Integration of South American Regional Infrastructure, both of which promise to promote the development of regional infrastructure and border areas.

These events are especially important because they lie at the very heart of the pursuit of development and a better life for our citizenry. In effect, we are witnessing more than just business initiatives: these moves aim to open markets for development of trade and foreign investment, which are among the few reliable external stimuli available to the region for institutional modernization, economic growth, and employment generation.

However, we must not lose sight of the fact that, by virtue of these negotiations, our borrowing countries find themselves facing challenges of historic proportions. This is because the initiatives will establish the principal regulatory frameworks and rules of the game for commercial, economic, and even political relations with neighbors and the rest of the world over the coming decades. Successfully rising to these challenges will create many opportunities for development and poverty reduction, while failure to do so would have significant negative repercussions.

The challenges are formidable because they encompass preparedness for multiple and substantively complex negotiations with industrialized countries that are well-equipped for this task, new institutional arrangements to implement comprehensive agreements that go beyond tariffs to domestic market regulatory issues, and the creation of a policy environment enabling businesses to exploit the new opportunities arising out of the expanded market while distributing benefits in an economically efficient and socially just way.

The Bank is aware of these challenges. We are giving technical and financial support to the FTAA negotiations as well as a significant number of the hemispheric cooperation initiatives. We are also actively supporting the Initiative for Integration of South American Regional Infrastructure and the Puebla-Panama Plan.

What I wish to emphasize here, however, is the capacity-building needed to face the national challenges outlined above. Trade is not an isolated economic activity but, as I said, a major catalyst for energizing structural reform, economic growth with equity, and employment. Hence, the first priority is that trade and integration be mainstreamed in each country's development agenda and that sufficient resources be channeled to front-line ministries. The Bank has financial services to supplement this effort, and I want to highlight one in particular: our new Trade Facility. This facility provides for expedited approval of loans of up to US\$5 million to modernize trade-related ministries to build capacity for effective negotiation and implementation of trade agreements as well as promotion of the exports and investment that those agreements facilitate.

Meanwhile, our regular lending programs and the Multilateral Investment Fund (MIF) are available to support the structural adjustments that will be necessary in order to take advantage of the opportunities and accommodate the costs. To encourage use of these services, we will enhance our country strategy papers and pipelines. The Bank wishes to accompany its member countries in these historic endeavors, and I would urge our Governors to encourage their ministries to draw on the Bank's Trade Facility to help them meet the immediate challenges. I would suggest that these loans be looked at not as a current budgetary expenditure, but rather as an investment in the future.

3. External Advisory Group

In May 2001, the President of the Bank invited a group of distinguished public figures and experts from the world of international finance and economic development to come up with ideas on the Bank's future strategy and role in the region in light of the ongoing debate on the role and relevance of multilateral financial institutions. The task took longer and was ultimately more complex than originally anticipated, in the wake of the tragic events of September 11th.

The group's ideas were summarized in preliminary form in document CS-3413 and submitted to the Governors for the nonregional member countries in Berlin in January 2002;

they were subsequently presented, informally, to the Executive Directors. The main conclusions and recommendations are to be presented to the Governors at a meeting of the Committee of the Board of Governors by Mr. José Ángel Gurría, who has coordinated the overall effort. The report took as its starting point the Bank's *institutional strategy*, which assembles the institution's core objectives—poverty reduction and enhancement of equity and sustainable growth—and structures its work around the four pillars in which the Bank possesses comparative advantages: social development, boosting of competitiveness, modernization of the State, and regional integration.

In line with these objectives and pillars, the report focuses on three main issues: (i) new global economic trends and emerging needs of regional member countries; (ii) the importance of ensuring a continuing and, ideally, a more prominent presence of the Bank in the region as one means of restoring confidence in the countries of Latin America and the Caribbean and mitigating risk for private investors; and (iii) the Bank as a central player in effectively supporting agreements for trade, integration, and cooperation. The report proposes a number of alternatives for leveraging the Bank's capital so as to expand financial and nonfinancial services in priority activities and sectors. Since all these issues will surely be the subject of in-depth discussions and consideration by the Board of Executive Directors, we feel it is useful that they be presented for the Governors' information.

B. New challenges emerging from the regional and global debate

1. The supply of regional public goods: a renewed challenge for the Bank

As we have said on other occasions, the Bank must renew itself if it is to remain relevant. Such relevance can only exist if the Bank's work provides effective assistance to the region's countries in solving problems associated with new local and international circumstances.

While striving towards its objectives, the Bank must also perform the role that falls to it as a member of the international financial community, helping to attain the broad development objectives pursued by that community. This includes those associated with the institution's indispensable participation in the production of so-called *public goods*, which have gained such a high profile in global public opinion.

A sound program that has well-defined priorities and is coordinated with other regional and international agencies could afford the Bank a new and much broader presence in remedying the region's social and economic problems and strengthening regional cooperation.

2. Millennium Development Goals for Latin America and the Caribbean

Renewing the Bank's operating tools is intricately linked to the functions and mandates conferred upon the Bank by the member countries. These mandates translate into a frontal attack on poverty and efforts to attain robust, equitable, and sustainable growth, as embodied in the Eighth Replenishment and the *institutional strategy* and reaffirmed by the Heads of State of the Americas at the Third Summit of the Americas in Quebec City.

Poverty reduction is one of the most crucial of the stated objectives and it is certainly a core focus of action within our ambitious social and economic development agenda, which includes efforts to ensure greater social equality and inclusion of social groups left behind by social and economic progress.

The Millennium Development Goals (MDGs)² have become a key benchmark in the debate on objectives to be pursued by the multilateral development agencies. Although the MDGs embody the priorities of the international community, these priorities need to be translated into specific targets that our countries can adapt to their individual circumstances and those of the region.

The countries will thus be equipped with a set of basic referents for identifying their own development targets for the medium and long term, aiding them to launch processes of dialogue and consensus-building on policy measures for achieving the stated targets.

We intend to systematically include discussion on development targets aimed at reducing poverty as part of our country dialogue process, so these targets can be reflected in each country programming paper.

² See *United Nations Millennium Declaration*, resolution adopted by the General Assembly at the Eighth Plenary Meeting, 8 September 2000.

C. Institutional efficiency

1. Country programming

We need to persevere in our efforts to bolster the programming function, as a means of ensuring optimal use of the new lending framework authorized by the Governors. By formulating a strategy for each country, Management has provided a solid platform for the Bank's decision-making, while the *country papers* have become the cornerstone for the institution's activities. The Bank's relationship with the countries is programmed on the basis of policy dialogues, which draw in turn on studies and analyses of the social and economic situation in each instance. The Bank needs to better focus its action and allocate more resources to deepen the social and economic analyses of all the countries, bringing specialized knowledge of the issues and options for solutions. To this end, during 2001 we strengthened the Research Department, endowing it with more resources so as to enhance its support for the preparation of strategies and technical studies.

During the year, Management submitted for the Board's consideration a new set of guidelines for preparing *country papers*, essentially to set out general principles, structure and content, and background requirements. It is hoped that these guidelines will help to identify more clearly the issues and sectors in which the Bank Group's support and collaboration could be most effective, while establishing a suitable framework for programming our financial and nonfinancial activities in the countries. With an eye to evaluating the impact of Bank-supported activities in each country, Management intends to fine-tune the quantitative and qualitative performance indicators contained in the *country papers*, as input for monitoring and evaluation of the impact of those activities.

2. Building evaluation capacity within the Bank and in the countries

At the meeting of the Committee of the Board of Governors held on 2-3 July 2001, the Governors called on the Board of Executive Directors to continue exploring and analyzing arrangements for enhancing the country dialogue, and continue monitoring and evaluating the effectiveness of the Bank's financing instruments.

The strategic importance of building evaluation capacity was enounced in the report on the Eighth General Increase in Resources, which urged the Bank not only to strengthen its own

evaluation capacity, but also to “promote and support in-country capacity-building and facilitate cooperation in evaluation activities with other development agencies.”³

The Bank addressed this and other issues in a paper submitted last October to the Board of Executive Directors.⁴ The paper maintained that building evaluation capacity would entail: (i) collaborating more actively with borrowers in conducting evaluations of Bank operations, harmonizing and—to the extent possible—using the borrowers’ own evaluation systems to determine the outcomes and impacts of Bank-funded programs and projects; (ii) expressly including evaluation-capacity building as a core element of the strategy for modernization of the State, promoting the adoption of processes that foster results-driven management; and (iii) ensuring that the Bank’s lending and other instruments include discussions of evaluation as a tool for enhancing good governance in Latin America and the Caribbean generally.

While the methodology used for evaluation is an eminently technical matter, its *raison d’être* and implementation can have political ramifications as well. This is because it generates information on the viability and outcomes of agendas pursued by governments, and because—when it is performed correctly and systematically—its outcomes constitute the main input for the resource-allocation process. Political implications can also flow from the fact that evaluation reduces information asymmetry between service providers and the citizenry.

From a practical standpoint, it must be acknowledged that rigorous evaluation mechanisms entail a number of risks that cannot be overlooked, such as the temptation to bias our actions towards pursuing results that are easier to obtain and measure, which of course are not always the most important ones. Only if we remain aware of these risks can we steer clear of them. Still, the risks associated with the evaluation process are well worth taking, and the institutionalization and continuity of evaluation should be assured. Indeed, the greatest risk today is the fear of failure.

3. Financial administration and capital adequacy

To help determine the appropriate levels of loss-provisioning and reserves in terms of credit risk in the Bank’s lending portfolio, Management has embarked on a study to develop an analytic credit-risk model to serve as a tool for modeling such risks appropriately.

³ Document AB-1704, paragraph 2.100

⁴ *Evaluation capacity building: Elements of an approach to the region* (document RE-252).

A study on capital adequacy is urgently needed, especially in the current setting where: (i) the Bank would be authorized to grant very rapidly disbursing emergency loans, which could have a significant impact on its portfolio composition; (ii) the contagion effect could have a strong impact on a significant portion of the portfolio; and (iii) shareholders are calling for resources to be used more efficiently.

Once the study has been completed and once Management is satisfied that the model is sound, it will prepare a document—to be presented for consideration by the Board of Executive Directors in the third quarter—containing recommendations on capital adequacy policy and loan-loss provisioning according to the parameters of the new model. Management will also look into the possible need to amend other financial policies in the event the Bank approves use of the new model.

4. Development effectiveness of the Bank's work

Far from being an objective, ensuring the development effectiveness of the Bank's work is exactly what the document entitled "Development effectiveness at the IDB" (document CS-3401) says it is: the very *raison d'être* of an institution such as the Bank. Evaluating what we do and how we do it are two intrinsic and inseparable facets of one and the same process.

One of the achievements we are most proud of is the consolidation during 2001 of an independent Office of Evaluation and Oversight (OVE) with the expertise to assist us in gauging the value and impact of the Bank's programs, projects, and services for the countries. This has been a gradual effort that has involved the Bank's managers and staff, borrowers, executing agencies of financed projects and programs, and especially OVE staff members.

Over the course of the year, Management and OVE examined a number of core issues in the Bank's development work, evaluating the system for monitoring projects in execution and reviewing the merits and limitations of the various tools the Bank uses to track the specific situation of each project in execution, pick up problems affecting performance of its portfolio, and learn lessons from completed operations as expressed in project completion reports. Out of Management's experience and OVE's timely review came a set of recommendations that will enable us to enhance the monitoring and evaluation instruments of individual projects.

Linking these projects' stated objectives to each country's development targets makes it possible to identify cause-and-effect relationships between the Bank's action and the

achievement of those country targets. Unless we measure development impact, we will not know if the resources invested in financial and nonfinancial services are generating the expected social and economic benefits.

Project objectives, however, are not limited to actions that produce quantifiable physical outputs. And as a result, measuring progress towards results often will entail qualitative judgments or the possibility of impacts that are not apparent in the short term because they involve hard-to-measure changes in the stock of nonphysical capital. This is a challenge for the Bank that will require not only an effort to harmonize processes, procedures, and incentives but also support for methodologies to adequately gauge the effectiveness of the Bank's work. Management has embarked upon this task with OVE, and we will coordinate our efforts in this regard with the other multilateral development banks.

Enhancing the effectiveness of the Bank's work does not mean just perfecting tools for monitoring and evaluation; it also means centering operations in a limited number of sectors in order to provide more robust and sustained support in areas where we have greater capacity to add value. By concentrating on a defined set of issues, we can identify outcomes better, and the likelihood of obtaining those outcomes will be increased by dint of transparency and accountability.

Embracing a results-driven approach is not without its difficulties. The "results" produced by an institution are a reflection of the objectives pursued and of institutional strengths and weaknesses. Accordingly, special emphasis needs to be placed on defining, in accordance with our mandate and identity, the kind of results we wish to obtain. Institutions that decide to measure their outcomes using benchmarks from elsewhere are doomed to mediocrity or loss of their identity. In other words, since the Bank is a unique institution, the indicators it uses to show the outcomes of its action must also be unique.

5. Priorities of the work program

To ensure that these priorities are duly reflected in the Bank's work, Management has proposed—and the Board of Executive Directors has agreed—that the 2002 work program will focus on the issues outlined earlier: lending instruments; enhancing the development impact of the Bank's programs and projects; making nonfinancial services more relevant and effective in line with institutional priorities; improving human resources management, which is crucial to

guaranteeing the quality of financial and nonfinancial services delivered by the Bank; and updating the Bank's financial risk management policies.

Management wishes to acknowledge the work of the Board of Executive Directors and its committees towards implementing these initiatives and enhancing efficiency. The committees have worked together closely within their respective spheres of responsibility, and this will surely have a positive impact on the relevance and effectiveness of the Bank's presence in Latin America and the Caribbean.