

THE WORLD BANK

OFFICE OF THE EXECUTIVE DIRECTOR

FOR:

**AUSTRALIA, CAMBODIA, KIRIBATI, KOREA (REP. OF),
FEDERATED STATES OF MICRONESIA,
MARSHALL ISLANDS (REP. OF), MONGOLIA,
NEW ZEALAND, PALAU (REP. OF), PAPUA NEW GUINEA,
SAMOA, SOLOMON ISLANDS AND VANUATU**



**ANNUAL REPORT
FINANCIAL YEAR 2005-2006**

September 2006

EXECUTIVE SUMMARY

During fiscal year 2006, our office continued to work on improving the World Bank Group's (WBG) planning and performance, to increase representation of our members' interests both at the Board and with Bank staff, and to assist our members in their overall relationships with the World Bank Group.

A little over a year after his appointment as Bank President, Mr. Wolfowitz completed appointments to his senior management team, and announced a Network Integration plan to realign the Bank's management structure to improve coordination and integration of operations across the World Bank Group.

Constituency Office

On 1 August, 2005 the office said farewell to John Austin and welcomed Dr. Joong-Kyung Choi from Korea as the new Executive Director. In addition, Joanna Gordon from New Zealand took up the Senior Advisor position; Chris Tinning, from Australia, replaced Julia Newton-Howes in the Advisor position; and on 1 March, 2006, Damba Baasankhuu from Mongolia, took up the Special Senior Advisor position vacated by Tom Hall.

Our office has continued to focus on improving communications with constituency members, especially developing country members. Our officers visited all but one constituency country in FY06 for consultations.¹ We have further developed the Office Newsletter summarizing relevant Bank issues every two months for government officials; we report to our authorities on Board matters, and regularly update our office website to facilitate broader public contact.

The office is trying to produce balanced opinion on the WBG's policy issues based upon the diversity in our constituency in terms of economic development and cultural background.

In our work at the Board and with management, we focused on improving governance in the Bank, in particular through better strategic planning, and containing growth in the Bank's budget (the cost of which is ultimately recovered from borrowers). Lowering the financial and compliance costs to developing countries of doing business with the Bank is important in keeping the Bank useful to its developing membership.

Our office has worked to raise the profile of three areas that we consider to be important priorities for the Bank: (a) Bank engagement in fragile states, that are lagging in progress towards the Millennium Development Goals, important in Africa and in the Asia-Pacific region; (b) the importance of country level work in the financial sector, including issues such as debt management capability and (c) the lack of Bank engagement in the product sectors or industrial base build-up which are essential for sustainable economic growth. "Even if we have well-educated healthy young people, they have no other choice than to migrate to neighbouring economies without a sufficient industrial base to absorb young labour forces". (ED Choi at the Board.)

We strongly urged the implementation of the FY06-FY09 Regional Engagement Framework for Pacific Islands. Our office has supported the Bank's work, stressing improving governance and the business climate in developing countries, and refining the use of performance and governance measures to allocate IDA resources.

¹ An intended visit to Kiribati had to be rescheduled to FY07.

Development Results

*From the start of his term, President Wolfowitz has emphasised improving outcomes from development assistance; his first major speech after assuming the Presidency, *Charting a Way Ahead: The Results Agenda*, was delivered at the 2005 Annual Meetings.² Some progress in Bank processes is apparent, for example, the significant number of Results-Based Country Assistance Strategies approved by the Board. But it remains true, as noted by the Independent Evaluation Group's 2005 Annual Report of Operations Evaluation, that much work remains to be done to institutionalise a 'results focus' among staff, particularly in global programs and sectors such as health.*

Bank Strategy and Leadership

The Bank continues to apply the strategy first adopted in FY02. The strategy, as applied in each year's Medium Term Strategy and Finance (MTSF) paper, centres around two pillars - investing in, and empowering poor people, and promoting a favourable investment climate. The direction is considered to be generally sound, with the challenge for the Bank continuing to be in the implementation process and defining priorities.

The MTSF for 2007-2009 is the first in the new President's term. A new senior management team has been appointed during FY2006. Their influence in refining the strategy may be seen in the next iteration of the MTSF.

IDA and IBRD Policy Issues

Large, performance-based soft loans and grants are now flowing under IDA14, and the Board discussed a review of IDA13 performance that was timely given the forthcoming IDA14 mid-term review (scheduled for November) and commencement of the IDA15 replenishment negotiations (scheduled for February 2007). The review highlighted a number of lessons learned during IDA13, including: (a) the need to improve measurement and monitoring of results at both the project and country level; (b) the importance of more effectively tailoring activities to country capacity; (c) the desirability of a clear performance-based allocation of grants; and (d) the need to clarify IDA's capacity to respond to exceptional circumstances outside of the Performance-Based Allocation system.

Efforts to improve the Bank operations in IBRD borrowers (mainly middle-income countries) were developed throughout the year and will be discussed at the 2006 Annual Meetings of Governors.

The Board's Committee on Development Effectiveness (CODE) considered an evaluation by the Bank's Independent Evaluation Group of the Heavily Indebted Poor Country (HIPC) initiative. This review confirmed that debt relief was not sufficient for debt sustainability. Other issues highlighted include: the need to improve debt management capability; the 'free-rider' issue; the importance of market and trade access in alleviating poverty; and the need to address the "lend and forgive" cycles.

IDA and IBRD finances

IBRD/IDA loans, grants, credits and guarantees for FY06 totalled \$23.6 billion, an increase of \$1.3 billion over FY05. Overall, IBRD/IDA lending commitments rose by 6 percent over the previous year.

²<http://intranet.worldbank.org/WBSITE/INTRANET/UNITS/INTPRESIDENTSTAFCONN/0,,contentMDK:20659654~menuPK:64259013~pagePK:64259040~piPK:64258864~theSitePK:1014519,00.html>

New IBRD loan commitments in FY06 increased to the highest volume in the past seven fiscal years growing to \$14.1 billion from \$13.6 billion in FY05. In FY06, IBRD operating income increased to \$1.7 billion from \$1.3 billion in FY05.

The Board approved the IBRD/IDA administrative budget in June 2006. The FY07 net administrative budget is \$1.6 billion, an increase of 3.1 percent over the FY06 budget. Total administrative expenses (including the budget for the Boards, the Development Grant Facility and the Staff Retirement Account) have increased by one percent from \$2.103 billion to \$2.119 billion. This lower rise compared to FY06 reflects reductions in pension contributions.

The IBRD's FY06 allocable net income was \$1.7 billion, and the Board will recommend to the Governors that \$500 million be transferred to IDA.

In FY06 IDA committed \$9.5 billion in new development assistance. Reflecting donor's high replenishment of IDA in IDA14, this commitment was the highest in IDA history. IDA credits outstanding at the end of FY06 were \$127 billion, compared with \$121 billion at the end of FY05, \$116 billion at the end of FY04 and \$107 billion at the end of FY03.

Operational Issues

Since former President Wolfensohn's 'Cancer of Corruption' speech in October 1996, the World Bank has sought to improve development outcomes from its (and other donors') aid by combating corruption in the use of its own funds, and helping governments of member countries to implement national programs that strengthen governance and discourage corrupt practices. President Wolfowitz has expressed determination to move the Bank to a more operational and proactive stance against corruption. He has strengthened the Department of Institutional Integrity to examine alleged corruption in Bank projects more quickly, and in some cases to assist national authorities with forensic auditing skills to help domestic investigations. In early 2006, he formed an internal review team to further develop and formalize Bank policy in combating corruption in its own projects, and to help strengthen governance in partner countries. This process of policy development was agreed to at the 2006 Spring Meeting by the Members of the Development Committee, and the proposed policy approach will be the key agenda issue at the September Development Committee meeting.

In FY06, the Bank continued to provide debt relief to the world's poorest and most heavily-indebted countries. Of the 40 countries currently covered by the HIPC initiative, 19 have reached completion point, 10 have reached decision point and a further 11 have yet to reach decision point. The HIPC eligibility deadline has been extended to 31 December 2006.

The Multilateral Debt Relief Initiative (MDRI) came into effect following careful work to shape the details of the scheme that enables IMF, IDA and African Development Bank debts owed by highly indebted poor countries to be forgiven. Following Board of Governors approval, the scheme came into effect on 1 July 2006 and \$18 billion of debt has been forgiven for nineteen completion point HIPCs.

The "free-rider" issue (i.e., unwise new lending into the borrowing headroom created by the MDRI) has been a concern of IDA deputies in the context of IDA14. The free-rider issue needs to be tackled from both a creditor and debtor perspective. Ultimately, the primary responsibility for debt management rests with the borrowing country. The debt sustainability framework (DSF) goes some way to deal with free-rider problems associated with concessional debt. For borrowing countries, a flexible case-by-case approach has been proposed countries are disciplined for excessive borrowing through a reduction in IDA volumes for 'red or amber light' IDA grant recipients and a hardening of terms for 'green light' IDA borrowers.

In 2005-06, the Bank continued its heavy involvement in Global Programs. The Bank supported more than 50 global programs with funding of over \$170 million.

In September 2005, the Development Committee endorsed an Africa Action Plan. The Plan aims to support African countries towards achieving the MDGs, reducing poverty and increasing growth. The Plan contains 25 initiatives and over 130 suggested actions focused in three broad areas: building capable states and improving governance; strengthening the drivers of growth; and increasing the effect of partnerships among governments, donor countries and development agencies.

Following a request from the G8 Meeting in Gleneagles, the Bank initiated work exploring increasing sustainable access of the poor to modern energy sources. After consideration of a preliminary paper at the 2006 Spring Development Committee meeting, the Bank has prepared a progress report for the Singapore Annual Meetings in September. The report examines the Bank's existing mechanisms for grants and loans and suggests they can stretch to address access and adaptation challenges, but that transition to a lower-carbon economy may require new instruments to help establish carbon markets.

International Finance Corporation (IFC)

The IFC generated a profit of \$1.5 billion in FY06, following the record profit of \$2.0 billion in FY05. The main source of the FY06 profit was net income of \$1.2 billion from equity investments, slightly lower than the \$1.4 billion in FY05. This resulted from the strong performance of equity markets in emerging countries and from investments in firms that benefited from high commodity prices, with associated high dividends and capital gains.

IFC's commitments signed during FY06 were \$6.7 billion, 25 percent higher than the \$5.4 billion of commitments signed in FY05 and in line with the Corporation's strong expansion plans endorsed in the Board's consideration of its Strategic Directions Paper for FY06-08.³

One of IFC's major achievements in the last few years has been its strong performance in the 'frontier markets' (defined as having a combination of low income and high risk, the latter measured by the Institutional Investor Country Risk Rating). In FY05, the share of commitments in frontier countries increased from 26 percent to 28 percent.

Since FY01, IFC's workforce has grown from 1,957 to 2,753 staff, a 41 percent increase. IFC hired around 630 staff in FY06, consistent with its strategic plans for expansion.

We cautioned, however, that the IFC is not focusing sufficiently on its core development challenges in frontier markets. We therefore emphasized the need for significant expansion of senior staff in frontier countries and encouraged IFC decentralization and enhancement of field-based project facilities. We suggested that IFC should focus on its comparative advantage to avoid poor quality control and unnecessary overlapping of business with other parts of the World Bank Group. In line with this, we believe IFC must ensure that the expansion and scope of TA activities do not detract from its core business.

Multilateral Investment Guarantee Agency (MIGA)

The size of MIGA's total gross guarantee portfolio has grown from \$5.09 billion in FY05 to \$5.36 billion in FY06. During FY06, the diversification of MIGA's guarantee portfolio has improved, with the share of

³ http://www.ifc.org/ifcext/about.nsf/Content/2005_Strategic_Directions_Paper

Europe and Central Asia contracts now slightly below the FY04 level and the share of financial sector contracts now below 30 percent.

The MIGA Board remains concerned about the need for continued diversification of the guarantee business for better development impact, a better understanding of the issues behind guarantee cancellations, and streamlining the technical assistance program of MIGA.

Constituency Country Developments

Australia: *In April, the Australian Government launched the first-ever 'White Paper' (or government strategic policy document), on Australia's overseas aid program: "Australian Aid: Promoting Growth and Stability". The White Paper will shape the delivery of Australia's aid over the next ten years and provides a comprehensive account of how the Australian Government will approach Australia's goal of doubling its aid budget to about \$A4 billion annually by 2010.*

The World Bank will be a prominent partner in implementing a number of the White Paper initiatives, particularly in the areas of infrastructure, results measurement and anti-corruption. Australia announced support for a number of key World Bank initiatives, including \$A1 million for the "Knowledge for Change" program and \$A500,000 for the Social Accountability Program.

Cambodia: *Achieving the priorities laid out in the Government's new five-year National Strategic Development Plan 2006-2010 (NSDP) is critical to Cambodia's success in the fight against poverty. The Eighth meeting of the Consultative Group on Cambodia discussed the NSDP and how development agencies can support the Government in implementing the key reform measures and development initiatives outlined in the Plan. The WB's Poverty Assessment 2006 found that while Cambodia has made greater progress than previously estimated in reducing poverty over the last decade, new and more complex institutional and policy changes and strengthened partnerships are needed if the country is to achieve its Millennium Development Goal of halving poverty by 2015.*

The Bank declared misprocurement in seven Cambodian projects and suspended disbursement in three. Notwithstanding the suspensions, the Board approved the Cambodia Public Financial Management and Accountability Project. The project aims to implement a ten year program of reforms to strengthen the Government's ability to formulate, execute and monitor its budget and to reform the civil service by introducing a merit-based staff selection, reward promotion system.

Korea: *Over the past year, Korea has continued to diversify and deepen its cooperative relationship with the World Bank both in its financial and non-financial aspects. Korea now intends to share its reservoir of experience and thereby assume a role, however modest, in the socio-economic advancement of developing nations and take an active part in international efforts to promote our common prosperity.*

The World Bank President, Mr. Wolfowitz, visited Korea in June 2006, accompanied by Executive Director Dr. Joong-Kyung Choi. He met the President of Korea, Moo-hyun Roh; Deputy Prime Minister and Finance and Economy Minister, Duck-Soo Han; Minister of Commerce, Sye-Kyun Chung; and Minister of Information and Communication, Jun-Hyung Roh. The visit provided an opportunity for Mr. Wolfowitz to discuss improvements in the partnership between the Korean government and the World Bank Group. Korea plans to double its total overseas development assistance from 0.06 percent of GDP to 0.1 percent of GDP by 2009. Korea will establish a \$30 million trust fund with the World Bank and a \$2 million trust fund with IFC. The Korea Consultant Trust Fund received \$465,000 this year. The Korean government's contribution to the Fund total \$5.2 million since its establishment in 1993. Korea has actively participated in the MDRI negotiations and has pledged to contribute SDR 249 million.

Mongolia: A technical meeting, jointly organized by the Government of Mongolia and the World Bank, was held in Ulaanbaatar, Mongolia, in late February 2006. The technical meeting marks a shift in the Government-external partner cooperation to better align external support with the government's own planning and budget cycle through regular six-monthly meetings focused on improving the management of development results.

Three IDA projects were approved in FY06, totalling \$26 million in grant. These were Governance Assistance; Rural Education and Development; and Information and Communication Infrastructure Development projects.

New Zealand: At the bilateral level, the past year has seen initiatives for deepening cooperation between New Zealand and the World Bank over a range of sectors and Pacific Member Developing Countries including the development of a health sector-wide approach (SWAP) in Samoa, an education SWAP in the Solomon Islands (preceded by a co-financed national skills survey), cooperation on a rural livelihoods program (also in the Solomon Islands), and exploring opportunities for collaboration in Vanuatu in the areas of private sector and rural sector development.

New Zealand has welcomed the World Bank's contribution to understanding current issues in the Pacific. Over the past year, this has included research on Pacific migration and remittance flows, a report on natural hazards management and the Pacific Infrastructure Report. New Zealand is also supporting the application in the Pacific of the World Bank's flagship global initiative on the Cost of Doing Business. NZAID is finalising a contribution \$200,000 to support the Bank's implementation of the Lao PDR Harmonisation Action Plan. NZAID is now contributing (NZ\$750,000 in 2005/06) to the Pacific Facility 3, joining the World Bank and AusAID in this initiative by the Bank to extend technical assistance to Pacific Island countries independent of lending operations and through a mechanism that can react more quickly and flexibly to needs within the region than those traditionally available through multilateral development banks.

Pacific Member Countries: Following FY05, Board endorsement of the Pacific Regional Engagement Framework FY06-09, a series of country-specific and regional lending, grant and advisory activities for Pacific member countries has been undergoing implementation, including newly planned projects to be submitted for Board approval. The activities support the Bank's strategy centred on two pillars-strengthening government capabilities in service delivery and improving incentives for private sector development.

The "Doing Business 2006 Creating Jobs Report" included all the Pacific member countries in our constituency. This report, third in a series of annual reports that examines member countries' business regulations, remains a useful analytical work and reference tool for Pacific member countries in improving their business climate.

With the Pacific and Caribbean member countries in mind, the Bank introduced a Concept Note "Small States Catastrophe Risk Insurance Facility" at the September 2005 Small States Forum, and substantial work is underway by Bank management to put in place the Facility that would allow all small states to buy insurance coverage against natural disaster risk.

Following the 2005 Small States Forum's deliberations that touched on a proposal to establish a small states network to facilitate dialogue among the 45 small states, the Bank has been exploring ideas with the Republic of Malta for setting up a network for improving knowledge and promoting good economic development policies in small states.

Papua New Guinea: *Currently, there are five Bank-assisted projects under implementation in Papua New Guinea. However, it is an aging portfolio with three of the five projects expected to close at the end of this year and a fourth in 2007, leaving only one under implementation thereafter. The PNG Government, with assistance from the World Bank, is continuing to implement the recommendation from the Public Expenditure Reform Review recommendations.*

The IFC implemented its first equity investment in PNG contributing to microfinance development.

Initial rounds of discussions with the PNG Government on the preparation of a new CAS were held early this year. The critical success factor for the Bank's CAS will be substantial dialogue with the government on its development agenda to be supported by the Bank during the four year period, 2007-2010. In the CAS, the Bank is anticipated to spell out the expected scale and scope of support for PNG. Authorities had requested the Bank to assist in impact projects like road infrastructure and productive economic sectors as outlined in the country's Medium Term Development Strategy.

CONSTITUENCY OFFICE

CONSTITUENCY OFFICE DEVELOPMENTS

During fiscal year 2006, the constituency office continued working to improve Bank planning and performance, to improve representation of the interests of our members at the Board and with Bank staff and to assist our members in their relations with the Bank.

Our office sought to further improve communications with constituency members, especially developing country members. Approximately every two months an Office Newsletter for government officials summarises the key policy developments at the Bank, use of Bank resources, and voice issues. We continue our regular electronic reporting on Board matters. We regularly update our office website (<http://www.worldbank.org/eds09>) for the benefit of civil society contact with us. We maintained active programs of visits to constituency countries. In FY06, our office made visits to all but one constituency member for consultations which improved our understanding of members' needs and increased our capacities to represent their views at the Bank Board and with management.¹ (see Annex 3).

On 1 August 2005 the office said farewell to John Austin and welcomed Dr. Joong-Kyung Choi from Korea as the new Executive Director. In addition, Joanna Gordon from New Zealand took up the Senior Advisor position; Chris Tinning from Australia replaced Julia Newton-Howes in the Advisor position; and on 1 March 2006 Damba Baasankhuu from Mongolia took up the Special Senior Advisor position vacated by Tom Hall.

Our office continued its support to the recently established secondment program for developing country officials. We informed constituency members about developments in this program and solicited candidates from them for calendar year 2007. An applicant from Solomon Islands was selected as one of the 24 secondees in the second cohort of the program.

POLICY ISSUES OF SPECIAL OFFICE INTEREST

Fragile States

Our office remains a strong voice for more effective Bank assistance to 'fragile states' - countries troubled both by serious poverty and weak governance. In January 2006, the Board reviewed progress made by the Bank in implementing its policies for so-called 'low income countries under stress' (LICUS); and in July, we contributed to a review by the Board's Committee on Development Effectiveness of an evaluation by the Independent Evaluation Group. By the Bank's definition, fragile states include Timor Leste, Cambodia and the Solomon Islands, and are home to a total of some half-billion of the world's poor. Many of this group are making the weakest progress towards the Millennium Development Goals (MDGs).

¹ An intended visit to Kiribati had to be rescheduled to FY07.

Our office acknowledges some progress in the Bank work on fragile states (particularly an improvement in the assessed quality and effectiveness of projects), but remains concerned that most small states have none or only one resident Bank representative. Consequently, the Bank continues to be poorly placed to understand the needs of these countries, to engage in trusted dialogue, and to deliver good-quality, timely assistance of the type the country would most value. The WB Quality Assurance Group's FY05 *Annual Review of Portfolio Performance* of February 2006 reported that the results of analytical and advisory reports are not being clearly disseminated and implemented in fragile states. Our office has joined with other directors who share these concerns to push for an improved effort by the Bank.

Financial Sector Strategy

Since the Asian financial crisis, there has been considerable growth in the resources the Bretton Woods Organizations have devoted to building capacity in the financial sector of developing countries. Most of that growth has been in the IMF and the IFC, rather than in the World Bank itself. Our office has expressed our concern that the resulting division of labour has not necessarily been logical or effective.

We consider that there are important public sector financial sector development challenges for which the World Bank, rather than the IMF or the IFC, remains the most effective provider. For example, in FY06, an Independent Evaluation Group report on lessons from the Heavily Indebted Poor Country (HIPC) Initiative, noted that eight out of the 13 HIPCs studied that had been granted debt relief had already re-accumulated debt to problematical levels. In 11 of those 13 countries, indicators of debt sustainability had deteriorated. It also noted there is no single part of the World Bank Group with the responsibility for improving debt management capabilities since the Bank's Treasury ceased providing that service in 2003 except for a fee. (In practice, it now provides the service mostly to middle income countries.)

Together with others, our office has pressed for a broad strategic review of how the Bank Group works in the financial sector, and of the respective roles for it and the IMF. President Wolfowitz announced in June 2006 some streamlining of Bank Group organization, including the merger of the Financial Sector Network with the Private Sector Development Network. We will continue to press for a proper strategic reconsideration of the role of the Bank in the financial sector as part of that merger.

Sources of Growth

Economic growth is fundamental to development and poverty reduction, and we have questioned whether the balance of Bank activities reflects the importance of growth and policies for growth. Appropriate means of promoting growth are very specific to country circumstances. We have asked whether the Bank is too formulaic in the prescriptions for growth outlined in Country Assistance Strategies.

Our office believes the Bank should pay more attention to the sources of growth most appropriate to country circumstances. We have pointed out the lack of Bank engagement in the productive sectors (or industrial base build-up) which is essential for sustainable economic

development. Thus, we are strong supporters of the independent high-level commission on Growth and Development announced by the President Wolfowitz in April 2006. The Commission which includes Duck Soo Han of Korea, will, over a two-year period, take stock of the current state of knowledge and understanding of economic growth, review the salient features of successful growth experiences, identify new and developing trends that are relevant to future growth strategies, and assess the most effective approaches for developing countries. The Commission is expected to shed light on the long-run forces underlying growth experiences and highlight the actions, at the national and international level, most likely to improve developing countries' growth prospects. The aim is to foster well-designed policies for shared and sustained growth that leads to improvements in the well being of the poor.

International Finance Corporation (IFC) Growth

Our office supported IFC's business strategies and its proposed budget. We cautioned however, that the IFC is not focusing sufficiently on its core development challenges in frontier markets. We therefore emphasized the need for significant expansion of senior staff in frontier countries and encouraged IFC decentralization and enhancement of field-based project facilities. We suggested that IFC should focus on its comparative advantage to avoid poor quality control and unnecessary overlapping of business with other parts of the World Bank Group. In line with this, we believe IFC must ensure that the expansion and scope of TA activities do not detract from its core business. We also noted that the development of financial sector is a critical factor for attaining sustainable economic development by mobilizing domestic resources. We argued that additionality should be a central factor in determining the rationale of IFC's involvement in any potential activity.

Bank- Fund Collaboration

The specialization and division of labour between the IMF and the World Bank Group have long been codified in a 'concordat' or memorandum defining the pattern of collaboration. On 29 March 2006, the IMF and the World Bank announced the creation of a six-member External Review Committee mandated by the World Bank President and the Managing Director of the IMF to examine the areas of Bank-Fund collaboration and propose improvements. The Committee is headed by Pedro Malan, the former Minister of Finance for Brazil, and includes Michael Callaghan, Executive Director in the Australian Treasury and formerly Executive Director on the IMF Board representing many of the countries of this constituency. Countries in this constituency have made submissions to the Committee, which is to make its final report by the end of 2006.

Our office has been actively involved in discussions with our counterparts on some of the issues being reviewed by the Committee, including the questions noted above on the respective roles of the components of the World Bank Group and the Fund in the financial sector; the role of the Fund in low-income countries; and the need for more autonomous engagement by each institution with member countries.

BANK GROUP STRATEGY AND LEADERSHIP

Development Results

From the start of his term, President Wolfowitz put a focus on achieving results among his top priorities. Mr. Wolfowitz's speech to the 2005 Annual Meetings, his first major speech after assuming the Presidency, was entitled "Charting a Way Ahead: The Results Agenda". In his speech, the President emphasized the need for the Bank to be accountable for delivering program that have a real impact on the day-to-day lives of the poor and the importance of addressing both qualitative and quantitative challenges in Bank program.

The President's attention to results gave further impetus to the Bank-wide results agenda which was launched in 2003. The Results Agenda includes actions across three pillars: in developing countries where results are achieved; in the World Bank itself through modifying key instruments to strengthen the results-focus; and across development agencies through harmonizing results-based approaches.

Steady progress against the results agenda is evident on a range of fronts, for example, the significant number of Results-Based Country Assistance Strategies approved by the Board. But the annual Independent Evaluation Group assessment concluded that much work remains to be done to institutionalise a results focus among staff, particularly at the thematic and global levels. Monitoring and evaluation continues to play second fiddle to project preparation, reflecting internal incentives to focus on disbursement rather than quality. IEG recommended that the management accelerate efforts to encourage both Bank staff and partner countries to focus on results through awareness raising, training and incentives.

The *FY05 Annual Review of Portfolio Performance* by the Quality Assurance Group (QAG), completed in January 2006, showed the proportion of Bank lending that achieved 'satisfactory or better' development outcomes has continued to recover and now stands at nearly 80 percent, the highest figure for 25 years. Regional performance is mixed, with East Asia and the Pacific achieving a healthy 81 percent but Africa and the Middle East and North Africa trailing at 72 percent. Performance at the sector level is also mixed, with private sector development and public sector governance work both showing slightly weaker performance than the portfolio average, and financial sector lending in the Bank continuing to decline.

The portfolio grew one percent in FY05, the first growth after five years of decline, although still \$21 billion below the FY00 peak. Approvals grew 12 percent with lending to fragile states and infrastructure accounting for the biggest increases. IDA approvals faced funding constraints in the last year of IDA13. Likely approvals will stabilize the portfolio at about \$100 billion in FY06-08, still about 25 percent below the 1999 peak in the wake of the Asian financial crisis.

The Review showed lending to fragile states remains the weakest part of the portfolio (with only 60 percent of project performances rated at satisfactory or better). The Review highlighted worryingly weak management of the LICUS portfolio, including low quality of supervision and lack of realism in detecting problem projects. However, efforts have been made to improve

portfolio quality and more recent evidence from the Independent Evaluation Group suggests a lift in project performance in fragile states.

Bank Strategy

The Bank continued to apply the strategy first adopted in FY02. The strategy, as applied in each year's *Medium Term Strategy and Finance* (MTSF) paper, centres around two main pillars - investing in and empowering poor people, and promoting a favourable investment climate. The direction is considered to be generally sound, with the challenges for the Bank continuing to be in implementation and defining priorities.

The MTSF for FY07-09 is the first in the new President's term. A new senior management team has been appointed during FY06. Their influence in refining the strategy may be seen in the next iteration of the MTSF.

This year, the MTSF highlighted the Bank's priorities as:

- Playing a pivotal role in aid coordination and maintaining focus on achieving results through better tailoring its assistance to the wide-ranging needs of its country partners. Specifically, the Bank is focusing efforts in Africa through its new Africa Action Plan, supporting both the G-8 initiative from June 2005 (now known as the Multilateral Debt Relief Initiative or MDRI), and African leaders in ensuring that the sizable increase in resources to the region is used efficiently and effectively.
- Redefining the Bank's role with IRBD clients who, despite their relative wealth, still have deep and varied development needs.
- Deepening Bank work on governance and anti-corruption.
- Building the Bank's global, knowledge-base by deepening its expertise in education, health, infrastructure, energy and sustainable development, and agriculture.
- Bringing together global priorities and country needs to not only ensure that links to country programs produce efficient gains, but also that the results of global programs are aligned with country outcomes. This priority relates to work such as measures to combat diseases prevalent across groups of countries (e.g., HIV/AIDS or malaria); regional or global environmental problems; or regional energy investments. The Bank's role in providing global public goods is also being re-examined.

These priority areas will be underpinned by a focus on results. The Bank has a two pronged approach; making linkages between outputs and outcomes through strategy and performance contracts as guide Vice Presidency Units, and by increasing resources to direct client services at the regional level and especially in Africa.

Our office has worked to raise the profile of three areas that we consider to be important priorities for the Bank: (a) Bank engagement in fragile states, that are lagging in progress towards the Millennium Development Goals, important in Africa and in the Asia-Pacific region; (b) the importance of country level work in the financial sector, including issues such as debt management capability and (c) the lack of Bank engagement in the product sectors or industrial base build-up which are essential for sustainable economic growth. "Even if we have well-

educated, healthy, young people, they have no other choice than to migrate to neighbouring economies without a sufficient industrial base to absorb young labour forces". (ED Choi at the Board.)

With respect to global issues, like the Avian Flu, the Bank has a convening and coordinating power that is unmatched. However, we consider it important that the Bank is careful not to spill over into operational efforts on global issues where other UN agencies have the comparative advantage.

Our office has continued to promote the view that the key implementation issues associated with the MTSF are:

- excessive and unsustainably rising costs, that are ultimately paid for by the Bank's clients;
- a continued need to progress the development of indicators of Bank performance and feedback mechanisms to decision-making. While some progress has been made in this area, we have particular concerns that work program agreements and, to some extent, strategy and performance contracts, may not be supporting the Bank's strategic priorities effectively. In the case of work program agreements, we are concerned that poor quality agreements are working counter to the achievement of intended priorities and strategies. The deficiencies in work program agreements have, in our view, been one of the reasons why rhetorical commitment by the Bank headquarters to work in fragile states has not converted to actual effort in some regions. We will continue to support efforts to develop tools that support the Bank's strategic direction and improved the management of resources;
- mandate creep. The office encourages the Bank to focus on intervening where it has the comparative advantage;
- economic and sector work that is not closely enough related to the needs of clients countries; and
- a generally improving the articulation of the trade-offs (including the areas where there will be either a gradual or specific exit).

Several of these matters are discussed elsewhere in this report.

Change in Bank Structure and Senior Management

By June of this year, a little over year since his appointment as the Bank President, Mr. Wolfowitz had appointed a senior management team and announced a Network Integration plan to realign the Bank's management structure to improve coordination and integration of operations across the Bank Group. Four of the previous six networks were consolidated into two; the Environmentally and Socially Sustainable Development and Infrastructure networks were merged into the new Sustainable Development Network; and the Financial Sector and Private Sector Development Networks were merged into the new Finance and Private Sector Development Network.

The two newly appointed Managing Directors (Messrs. Daboub and Wheeler) have assumed responsibilities for a mixture of regional and network responsibilities.

Juan José Daboub, formerly El Salvador's finance minister, formally took up his duties on 1 July 2006. Mr. Daboub has been given management responsibility for three regions, Africa, Middle East and North Africa, and East Asia and the Pacific. He will also be responsible for the Sustainable Development and the Human Development networks.

Mr. Graeme Wheeler from New Zealand, and former WB Vice President and Treasurer, is responsible for Europe and Central Asia, South Asia, and Latin America and the Caribbean, the Poverty Reduction and Economic Management, Financial Sector and Private Sector Development networks.

Our office looks forward to working with Mr. Daboub in East Asia and the Pacific, particularly in our constituency countries.

IBRD and IDA

Enhanced Support to Middle Income Countries

Bank management continues its efforts to improve the performance of the IBRD in accord with the Middle Income Country Action Plan, originally endorsed at the 2004 Spring meetings. During FY06, the Bank worked to prepare a paper for the Annual Meeting in Singapore in which it foreshadows specific decisions for Board consideration during FY07. The Bank is considering its role in four business segments: strategic policy advice; financial services; knowledge services; and private sector operations. Management continues to streamline internal Bank procedures to reduce the non-financial costs of doing business with the Bank; offer more competitive and transparent loan pricing; expand sub-national financing; and provide more timely knowledge services.

IDA Developments

Large, performance-based soft loans and grants are now flowing under IDA14, and the Board discussed a review of IDA13 performance that was timely given the forthcoming IDA14 mid-term review (scheduled for November) and commencement of the IDA15 replenishment negotiations (scheduled for February 2007). The review highlighted a number of lessons learned during IDA13, including: the need to improve measurement and monitoring of results at both the project and country level; the importance of more effectively tailoring activities to country capacity; the desirability of a clear performance based allocation of grants; and the need to clarify IDA's capacity to respond to exceptional circumstances outside of the performance-based allocation system.

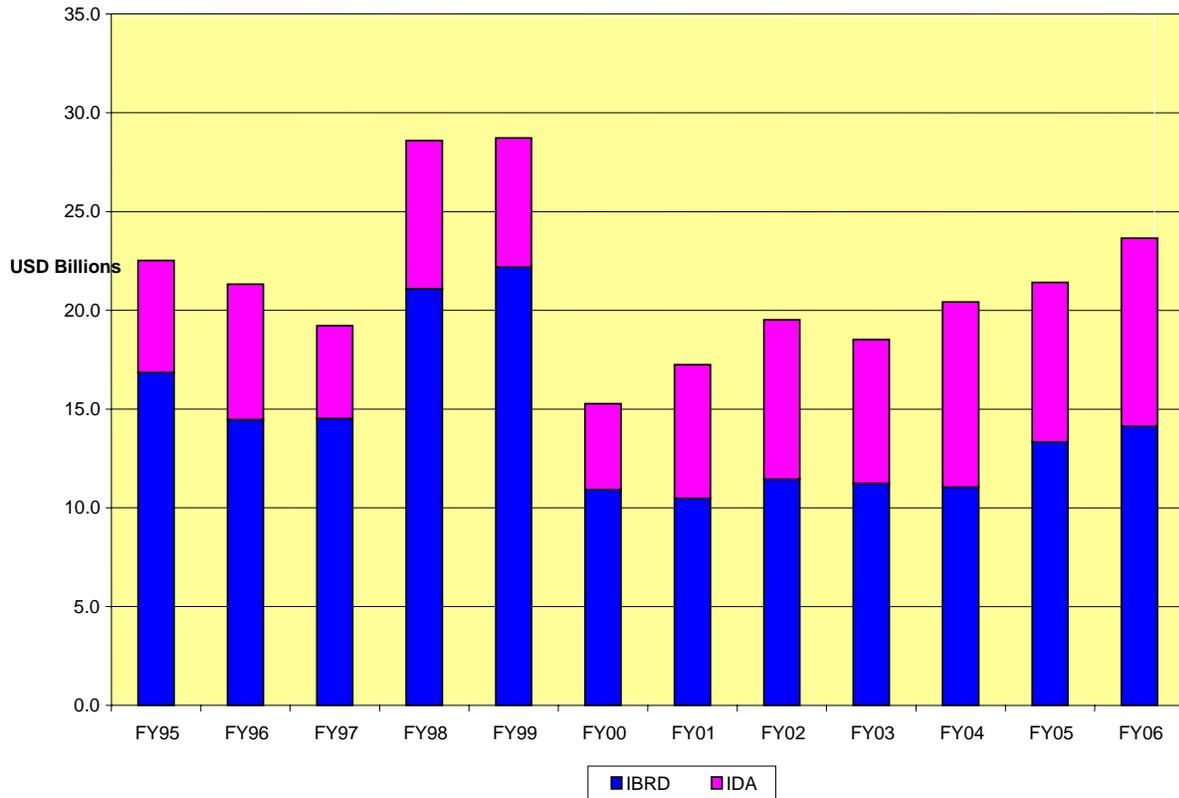
Trends in the IBRD and IDA lending portfolios

IBRD/IDA loans, grants, credits and guarantees for FY06 totalled \$23.6 billion, an increase of \$1.3 billion over FY05. Overall, IBRD/IDA lending commitments rose by six percent over the previous year. FY06 saw a total of 279 IBRD/IDA lending and guarantee operations delivered.

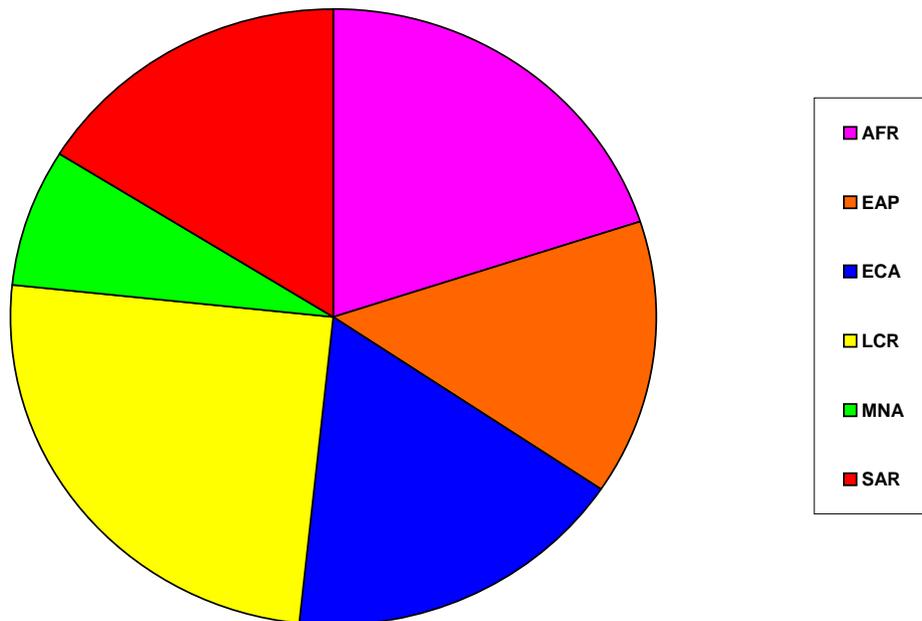
Of the IBRD/IDA total, \$16.3 billion (or 69 percent) was for investment operations while the remaining \$7.3 billion (or 31 percent) was for policy based operations.

In terms of where the IBRD/IDA lending went in FY06, Latin America and the Caribbean (LAC) received \$5.9 billion (26 percent), followed by Africa (AFR) with \$4.8 billion (20 percent), Europe and Central Asia (ECA) with \$4.0 billion (17 percent), South Asia (SAR) with \$3.8 billion (16 percent), East Asia and Pacific (EAP) with \$3.4 billion (14 percent), and Middle East and North Africa (MNA) with \$1.7 billion (7 percent). It is noteworthy that Africa IBRD/IDA lending commitments rose 23 percent from FY05 to FY06.

IBRD/IDA New Commitments, FY95-FY06



IBRD/IDA Commitments by Region FY06



The top ten IBRD/IDA borrowers represented over 50 percent of loan commitments in FY06. Mexico and Brazil were the largest borrowers, with Turkey, Pakistan and China rounding out the top five country clients.

New IBRD loan commitments in FY06 increased to the highest volume in the past seven fiscal years growing to \$14.1 billion from \$13.6 billion in FY05. A total of 112 IBRD lending and guarantee operations were delivered in FY06. The share of investment lending compared to development policy lending remained high at 65 percent of total commitments, most likely reflecting the continued emphasis on infrastructure lending that is part of the Bank's strategy for improving its performance in middle-income countries.

In spite of the increasing growth in new lending, FY06 was another year of negative net disbursements: some \$2.1 billion for the IBRD portfolio, down from \$5.1 billion in FY05. Loans outstanding at end FY06 totalled \$102.6 billion. As in previous years, the reason for the negative net disbursements are prepayments of older, higher cost IBRD "pool loans" by middle income borrowers, who now have access to cheaper commercial loans. (See discussion in following section.) The five countries to which IBRD has the highest exposure at end FY06 are China, Brazil, Mexico, Indonesia, and Argentina.

IDA credits outstanding at the end of FY06 were \$127 billion, compared with \$121 billion at the end of FY05. In FY06 IDA committed \$9.5 billion in new development assistance, the highest in IDA history. New IDA commitments in FY06 continued to concentrate mainly in the African region, rising 23 percent from FY05 to FY06, while commitments to East Asia and the Pacific rose **nine** percent during the same period. In FY06 IDA commitments delivered 167 IDA lending and guarantee operations.

Analytic and Advisory Assistance (AAA)

There were fewer Economic and Sector Work (ESW) and Technical Assistance (TA) deliveries in FY06 compared to FY05, with 601 ESW products and 307 TA activities by year-end, compared to 694 ESW and 351 TA deliveries in FY05. This reflects the consolidation of AAA tasks into larger pieces of analytic work. The consolidation initiative is intended to optimize resources, improve management oversight, and prevent fragmentation of non-lending activities.

A total of 31 Country Assistance Strategy (CAS) documents were delivered, including Interim Strategy Notes, (ISNs), for Iraq, Kosovo and Afghanistan. ISNs are prepared when a full CAS cannot be completed due to specific country circumstances. CASs for Bangladesh, Uganda, and Georgia looked to work collaboratively with other partners. Overall, 17 CAS products were produced jointly with IFC.

In FY06, 30 Poverty Reduction Strategy Papers (PRSP) were discussed by/distributed to the Bank Board. Overall, the number of countries with full PRSPs continues to rise and has now reached 50. The Board also discussed the second generation full PRSP documents for Ghana, Tanzania, Uganda and Nicaragua.

At the end of FY06, 29 countries are benefiting from debt relief under the HIPC Initiative. The Board discussed a total of four HIPC documents for African countries in FY06.

FY07 Administrative Budget

The Board approved the IBRD/IDA administrative budget for FY06-07 in June 2006. The FY07 net administrative budget is \$1.6 billion, an increase of 3.1 percent over the FY06 budget. Our office is again pleased to note that both the compensation adjustment and the remaining administrative budget increase were lower than in previous years, in line with management's stated target of achieving zero real growth in Bank expenditure over the next three years².

Total administrative expenses (including the budget for the Board, the Development Grant Facility and the Staff Retirement Account) have increased by one percent from \$2.103 billion to \$2.119 billion. This lower rise compared to FY06 reflects reductions in pension contributions.

IBRD Net Income Results

In FY06 operating income increased to \$1.7 billion from \$1.3 billion in FY05.

\$ Millions

	FY06	FY05	Variance	percent change
Income from Loans	4,864	4,155	709	17
Income from Investments, net	1,057	627	430	69
Other Income	267	271	(4)	(1)
Total Income	6,188	5,053	1,135	22
Borrowing Expenses	3,941	3,037	904	30
Administrative Expenses	1,055	1,021	34	3
Contributions to Special programme	173	173	-	0
Release of Provision for Losses on Loans and Guarantees	(724)	(502)	(222)	44
Other Expenses	3	4	(1)	(25)
Total Expenses	4,448	3,733	715	19
Operating Income	1,740	1,320	420	32

- Income from loans increased by \$709 million, mainly as a result of higher average lending rates. Bank borrowing expenses increased by \$904 million, reflecting higher average interest rates.
- The release of provisions was \$222 million more than in FY05 reflecting improvements in the quality of the Bank's portfolio as well as higher interest rates being earned on loans and equity.
- Administrative expenses increased by \$34 million reflecting an increase in post-retirement benefit expenses and an increase in share ratio in FY06.

² The zero-real growth target is to be achieved within a framework that will allow management a two percent "flexibility band" around the budget target. This is intended to be a tool to manage timing mismatches between the implementation of new initiatives and offsetting savings, while achieving zero real growth over the course of the these years.

- The return on equity (using allocable net income) for FY06 was 5.1 percent. This is an improvement on the 3.5 percent reported in FY05, although not yet at the high level of 9.1 percent in FY03.

Phase Out of Pool Loans

It is proposed to offer borrowers in the currency and pool loan programs a choice to convert to a more transparent lending rate that is lower than the high and rising interest rates in these programs. This would save borrowers about \$900 million in interest charges. There are two main reasons behind this offer, fairness and managing the risk to IBRD's income from pre-payments.

The proposal is expected to reduce IBRD loan income by \$100 million per annum over the period of 2007-2015. As IBRD will face the costs associated with prepayments in any case, the costs of the proposal are roughly the same as the costs of taking no action on phasing out pool loans.

Net Income Allocation

IBRD's FY06 allocable net income is **\$1.7 billion**, and the Board has recommended that Governors approve the following allocation at their meeting in Singapore:

<u>Allocable net income (millions)</u>	<u>1,676</u>
Released loan loss provision to reserves	724
Additional to reserves	312
Non-earmarked surplus	140
Transfer to IDA	500
Extraordinary transfer to IDA	300

- The transfer to IDA (IDA14) is part of a \$1.5 billion commitment over three years.
- The extraordinary transfer to IDA from earmarked surplus is outside the \$1.5 billion.
- There is no new allocation in FY06 to earmarked surplus. There is a non-earmarked surplus of \$200 million. The extraordinary transfer to IDA (\$300 million) will use all the funds that were in earmarked surplus, reducing the balance to zero.
- The loan charge waivers have been changed, with the front-end fee being fully waived on IBRD through the waiver increasing from 75 to 100 basis points. Other loan charge waivers have been retained at their current levels.
- The transfer to HIPC of \$210 million in FY05 completed IBRD's 1996 pledge to provide a total of \$2.15 billion in debt relief in 1998 NPV terms which is why no transfer is suggested for this year.

IBRD Capital Adequacy

Since 2003, IBRD's capital adequacy position has continued to improve. This year's improvement continued to be the result of improvements to the loan portfolio that are more

structural in nature, largely influenced by improved borrower credit ratings and countries moving from non-accrual to accrual status.

Capital adequacy is a measure of the probability of a call on its callable capital. It is measured by two indicators. The first, the equity-to-loans ratio, has risen to 33.1 percent which is 1.7 percentage points higher than the FY05 result. The second indicator, a stress test, shows that IBRD's ability to continue to generate earnings in the case of a credit shock (and hence continue to provide assistance to developing countries), has continued to improve in FY06.

OPERATIONAL ISSUES

Governance and Corruption

Ever since former President Wolfensohn's "cancer of corruption" speech in October 1996, the World Bank has sought to improve development outcomes from its (and other donors') aid by combating corruption in the use of its own funds, and helping governments of member countries to implement national programme that strengthen governance and discourage corrupt practices.³ The Bank has defined "corruption" as the abuse of entrusted power for private gain; "governance" is the broad set of arrangements by which a state acquires and exercises the authority to provide and manage public goods and services. Thus, corruption is often a symptom of weak governance and is highest (and often pervasive) where governance processes are weakest; for example, poor fiscal and audit systems and weak institutions to provide checks and balances on the abuse of authority, and accountability in the use of public finances. When corruption occurs in stronger governance environments, transparency in fiscal systems, accountability (such as through auditors, courts and parliament) and checks and balances (such as independent media) usually work to punish the offence.

Since late 2005, there have been a number of high-profile cases where alleged corruption in the use of Bank funds caused delays in disbursement of Bank loans, or in the President's recommendations to the Board for approval of new Bank loans or grants. The delays allowed fiduciary designs to be tightened, or other corrective actions to be launched. Cases during FY06 included Chad, Kenya, Argentina, India, Bangladesh, the Republic of Congo, Ethiopia, Indonesia, Angola, Bolivia and Cambodia. Executive Director Choi visited Cambodia to discuss the issue with Cambodian authorities and discussed associated issues with President Wolfowitz.

President Wolfowitz has expressed determination to move the Bank to a more operational and proactive stance against corruption. He has strengthened the Department of Institutional Integrity to examine alleged corruption in Bank projects more quickly, and in some cases to assist national authorities with forensic auditing skills to assist investigations. In early 2006 he formed an internal review team under the leadership of Managing Director Graeme Wheeler to further develop and formalize Bank policy in combating corruption in its own projects, and to help strengthen governance in partner countries. This process of policy development was agreed by Governors at the 2006 Spring Meeting of the Development Committee, and its results will be the key agenda item at the September Development Committee meeting.

Our office has played an active role in the development of the policy paper, drawing on experience within our constituency. We have emphasized that the Bank's key mission must remain poverty alleviation and the Bank, therefore, needs to stay constructively engaged in poor countries where corruption may be high and governance weak. We particularly stressed the need for the Bank to improve its engagement in fragile states, which by definition are both very poor, and have weak governance environments.

³ *People and Development*, Annual Meetings Address 1 October 1996, James D Wolfensohn; see <http://web.worldbank.org/WBSITE/EXTERNAL/NEWS/0,,contentMDK:20025269~menuPK:34472~pagePK:34370~piPK:34424~theSitePK:4607,00.html>.

Debt Sustainability Framework (DSF)

The Bank and IMF have developed a framework (the DSF) that is intended to prevent the debt of developing countries reaching unsustainable levels. The DSF involves identifying how much debt a country can afford according to its economic circumstances, policy and institutional performance, and vulnerability to economic shocks. The Bank and the IMF, in consultation with other creditors, also explore alternatives to debt financing for countries whose debt is approaching an unsustainable level.

In its April 2006 review of the DSF, the Board recognised that the DSF is sound and a good basis to work from, with support for its current threshold levels. There are areas where the DSF will be improved including the integration of domestic debt within the framework, considering more broadly both concessional and non-concessional debt accumulation, looking at how the DSF deals with those countries on the margins between IDA grants or loans, and addressing free-rider problems (further discussed below).

Heavily-Indebted Poor Countries (HIPC) Initiative

In FY06, the Bank continued to provide debt relief to the world's poorest and most heavily-indebted countries. Of the 40 countries currently covered by the HIPC initiative, 19 have reached completion point, 10 have reached decision point and a further 11 remain pre-decision point. Reaching completion point will enable these countries to receive the full amount of debt relief promised at decision point as well as becoming eligible for the MDRI.

The HIPC eligibility deadline was extended to 31 December 2006, through extension of the so-called Sunset Clause. Without any other action being taken, after 31 December 2006 no new countries will be eligible for HIPC treatment. IDA is currently preparing options for HIPC eligibility for the Board given the imminent expiration of the Sunset Clause. These options will be decided upon before the end of this calendar year.

The Board's Committee of Development Effectiveness (CODE) considered an evaluation of the HIPC initiative prepared by the Bank's Independent Evaluation Group. This important review identified, among other things, that debt relief was not sufficient for debt sustainability, the importance of ensuring that good performers – HIPC and non-HIPC – were rewarded, the need to improve debt management capability, the need to manage the free-riding, the importance of market and trade access in alleviating poverty and the need to address “lend and forgive” cycles.

This office has raised both debt management and the importance of rewarding good performers (HIPC and non-HIPC) in this context, as well as in others (e.g. the Medium Term Strategy and Finance, and Budget discussions). As we noted in our last report, the reward of good performers, irrespective of their HIPC status, is a concern to our constituency, since the better-performing countries of the Asia-Pacific region would be disadvantaged if HIPC resource flows, directed mainly to Africa, reduced aid-flows to non-HIPC countries.

Multilateral Debt Relief Initiative (MDRI)

In June 2005, the G8 asked the Boards of the Bank and the IMF to consider a total debt relief proposal. This MDRI has been strongly supported within this constituency, as well as more broadly.

The MDRI came into effect following careful work to shape the details of the scheme that enables the IMF, IDA and African Development Bank debts owed by the highly indebted poor countries to be forgiven. Following Board of Governors approval, the scheme came into effect on 1 July 2006 and \$18 billion of debt has been forgiven for 19 post-completion point HIPC countries. Seventeen post-decision point HIPC countries will become eligible for the MDRI when they reach completion point, with one further country becoming eligible once it satisfies the required criteria. A further 14 pre-completion point HIPCs were identified as potentially eligible for the scheme under a ring-fencing arrangement, although only 11 of these countries will participate in this arrangement.

The MDRI is a very long-term commitment covering 40 years. This has significant implications for IDA finances. The costs of the MDRI are being met by additional contributions by donors, made under different legislative and parliamentary arrangements in different countries.

This office has conveyed our authorities' view that debt relief should also be available to highly indebted poor countries that are not classified as HIPCs. The office intends to work on gaining wider support for such an idea.

Managing Free-rider Concerns

The free-rider issue has been a concern of IDA deputies in the context of IDA14, as well as the MDRI, and is a concern shared with many others who do not want to see countries becoming debt distressed. The free-rider problem has two dimensions. Lenders can thwart the intentions of IDA and MRDI debt relief by lending on non-concessional terms to countries, pushing them back into debt distress. There is also a moral hazard problem where countries become re-indebted following debt relief. The free-rider issue needs to be tackled from both a creditor and debtor perspective. Ultimately, the primary responsibility for debt management rests with the borrowing country.

The DSF goes some way to deal with free-rider problems associated with concessional debt. However, other options have been developed to manage the non-concessional debt build-up where lenders may not be MDBs, or may not ascribe to the DSF. For borrowing countries, a flexible case-by-case approach has been proposed where, as an ultimate discipline on excessive borrowing, a reduction in IDA volumes for 'red or amber light' IDA grant recipients, and a hardening of terms for 'green light' IDA borrowers. The Bank and IMF would also work together on widening the use of the DSF and coordinating creditors.

Bank's Role in Global Program/Avian Flu

The Bank continued its heavy involvement in Global programs in 2005-06. The Bank supported more than 50 global programs worth over \$170 million. The portfolio included global public goods such as: combating communicable diseases (HIV and the Avian Flu); preserving the environment (climate change, fragile or unique ecosystems); trade integration; and acquiring and sharing knowledge from research activities. However, the Bank was also involved in many global initiatives with no clear-cut global public goods dimension, they are education, infrastructure, international migration, and fostering peace and security.

Our office recognizes that the Bank has an important role to play in global programs, but we are working to ensure that core Bank programs at the country level receive adequate attention and the Bank does not stray into areas where other international agencies are better placed to assist. Therefore, in our Board interventions we stressed the need for the Bank to focus on those global programs in which it had a comparative advantage and to coordinate closely with other relevant international agencies.

The Avian Flu preparations represent the Bank's most prominent new global program. Following requests from major shareholders, the Bank took a leading role in coordinating the global response to the Avian Flu, including convening a series of major conferences, most prominently the January donor pledging conference in Beijing. Just prior to the Beijing conference, the Bank Board approved a \$500 million facility designed to provide fast and flexible support to Avian Flu prevention measures in both IDA and IBRD countries.

Statistical Capacity Building

Weaknesses in national statistics limit the ability of both national governments and their development partners to implementing policy reforms, to measure success and correct mistakes. The need for improvements in national statistical systems is an element of the World Bank's strategy for implementing the results agenda. An action plan known as the Marrakech Action Plan for Statistics (MAPS) was agreed in February 2004.

In May 2006, the Board noted that some progress is being made in working towards the principal objectives of the MAPS. MAPS implementation will need continued strong support from the Development Grant Facility, continued promotion of statistical capacity improvement at country level, and resources for country level planning through the Trust Fund for Statistical Capacity Building. This Trust Fund was recently restructured, extending its original December 2005 closing to 2010. It is now open for applications for grants to support statistical capacity building projects, and our constituency members could benefit from applications under this scheme

Voice

The past fiscal year has seen further work in enhancing the voice and participation of developing and transition countries' decision making - a call made by the Development Committee each year since the 2002 Monterrey Consensus.

The Voice Secondment Program approved by the Board in April 2004 as a five-year program has been successfully implemented. Representatives from our constituency countries have been participating in each cohort of the program to date. The second cohort of the program in FY06 included an official from the Solomon Islands.

Fundamental consideration of influence in the governance of the Bretton Woods Institutions is currently focused on the IMF's quota arrangements. New proposals will be considered at the 2006 Singapore meeting of the IMFC.

Clean Energy for Development and Climate Change

During FY06, and following a request from the G8 meeting in Gleneagles, the Bank initiated work exploring increasing access of the poor to modern energy. At present, 2.4 billion people rely on biomass fuels (wood, agricultural residues and dung), causing some two million premature deaths a year, about four percent of the global burden of disease. Access to modern energy forms could also assist mitigation of global warming under some conditions by helping stabilize carbon emissions. It is also important to facilitate adaptation to whatever global warming occurs after feasible mitigation.

Following consideration of a preliminary paper at the Spring Development Committee meeting, the Bank has prepared a progress report that will be background documentation at the Singapore DC Meeting in September. The report examines the Bank's existing mechanisms for grants and loans, and concludes they can stretch to address access and adaptation challenges. But the Bank continues to explore whether it can contribute through new financing vehicles to the development of a carbon market that would help ensure that very strong growth in energy consumption (e.g. from coal-fired electricity generation in China and India) was consistent with mitigation of global warming.⁴

Our office remains active in these issues, with particular attention to the interests of the Pacific constituency members who are potentially vulnerable to the effects of global warming and have a strong interest in the adaptation program.

Africa Action Plan (AAP)

In September 2005, the Development Committee endorsed an Africa Action Plan. Underlying the Plan is a message that Africa ought to benefit from a shared growth agenda. The Plan aims to support African countries in achieving their MDGs, reducing poverty and increasing growth. The results-oriented Plan contains 25 initiatives and over 130 suggested actions focused in three broad areas: building capable states and improving governance; strengthening the drivers of growth; and increasing the effect of partnerships among governments, donor countries and development agencies.

⁴ Some ideas in this area involve the World Bank making soft loans to finance the use of higher-cost but carbon-efficient technologies in developing countries, in return for both loan repayments and the title to 'carbon credits' from the use of the technologies, which the Bank could then sell to others. The ideas remain tentative, as such schemes are closely bound up with any post-2012 regulatory foundations for carbon trading that would influence the supply and demand of carbon credits and thus affect their value.

In addition to the Plan itself, there has been work to develop a proposed Africa Catalytic Growth Fund (ACGF) through which donors could increase assistance to Africa by augmenting IDA assistance and potentially providing project and program assistance more rapidly. The ACGF would also help overcome some of the difficulties that may be encountered in using IDA funds to support regional initiatives. This specific problem is not unique to Africa and we would encourage it to be addressed for all IDA eligible/fragile states, where the ACGF could be seen more as a pilot. Once evaluated, the positive features of the proposed ACGF (i.e. a focus on high performing and transition countries, and regional initiatives) could be extended more widely to other IDA countries.

Trade

Access to global markets has been an important tool of economic development, but developing countries need the capacities to trade competitively in order to take advantage of market access, without high costs and delays from poor infrastructure or administration. The current efforts on aid for trade are to significantly scale it up and to make it more effective, through an enhanced Integrated Framework (IF) for Trade-Related Technical Assistance. The IF aims to strengthen and streamline the trade-related assistance delivered by the Bank and five other agencies. The recent suspension of negotiations in the Doha Development Round does not detract from the logic behind aid for trade.

An update on the Bank's work on trade issues, including aid for trade, will be presented as a background paper to the Singapore meeting of the Development Committee.

A key tool in analysing needs is the Diagnostic Trade Integration Studies. By FY06, Diagnostic Trade Integration Studies had been completed in Cambodia and Mongolia. In Cambodia, a project building capacity for trade negotiation is under way. Vanuatu has applied to the Integrated Framework, with likely assistance being provided through the UNDP.

IFC and MIGA

International Finance Corporation (IFC)

IFC continues a phase of rapid growth in accord with its strategic priorities, to increase its development impact and respond to the needs of its member countries.

Strategic priorities

Over the period FY07-FY9, IFC aims to scale-up and accelerate implementation of the five strategic priorities, endorsed by the Board in April 2004:

- strengthening the focus in frontier markets (defined as having a combination of low income and high risk, the latter measured by the Institutional Investor Country Risk Rating);
- building long-term partnerships with emerging global players in developing countries;
- differentiating itself from other potential investors through its sustainability competencies;
- addressing constraints to private sector growth in infrastructure health and education; and
- developing local financial markets through institution building and by the use of innovative financial products.

In addition, IFC established six key corporate goals to be achieved over the FY07-FY09 period:

- delivering on development impact by focusing on priorities including Sub-Saharan Africa and Middle East and North Africa;
- increasing World Bank Group cooperation;
- showing leadership in standard-setting, particularly in environmental, social and corporate governance fields;
- achieving greater client satisfaction, with further decentralization and process and productivity improvements;
- maintaining a sound financial framework, including additional focus on risk management where IFC is undertaking an extensive review; and
- building and keeping a strong, diverse and motivated staff.

Frontier issues

One of IFC's achievements in the last few years has been its strong performance in 'frontier markets'. In FY06, the share of commitments in frontier countries increased from 26 percent to 28 percent. This percentage is forecast to increase to around 34 percent for the whole of FY07.

IFC's Operational Results

IFC generated a record profit of \$1.5 billion in FY06, compared with the then-record profit of \$2.0 billion in FY05. The main source of the FY06 profit was the net income of \$1.2 billion from equity investments, compared with \$1.4 billion in FY05. This resulted from the strong performance of equity markets in emerging countries and from investments in firms that benefited from high commodity prices, with associated high dividends and capital gains. Income is expected to be lower in FY07 mainly due to a return to normal levels of equity income. IFC's commitments signed during FY06 totalled \$6.7 billion, 25 percent higher than the \$5.4 billion of

commitments signed in FY05. IFC is forecasting an increase in its annual commitment volume to a range of \$7.0 to \$8.2 billion by FY09. Overall commitment targets are expected to increase by nearly 90 percent over the FY04 to FY09 period.

The quality of IFC's portfolio has continuously improved since FY02, when the Argentine crisis struck IFC. At the end of June 2006, IFC's total reserves for losses were \$0.9 billion, down from \$1.0 billion at the end of FY05. At June 30, 2006, the accumulated reserve for losses on guarantees, included in the consolidated balance sheet in payables and other liabilities, was \$18 million, compared with \$13 million in FY05.

Net Income Allocation

FY06 allocable net income was \$1.278 million and the Board will recommend to Governors at the Annual Meetings that it be allocated as follows:

Allocable net income (Millions)	1,278
Designation to IDA	150
Designation to TAAS	230

The unprecedented proposal of a \$150 million allocation to IDA proved to be controversial. A number of EDs supported the proposal, although their motives and levels of enthusiasm differed. Our Chair supported the proposal because use of the funds by IDA was preferred to IFC expanding its business into areas where it had less comparative advantage. Some chairs did not support, or were uncomfortable with, the \$150 million allocation to IDA, despite their general support of IDA. One of the concerns was that the proposed arrangement potentially confused the roles of both IDA and IFC.

This represents another chapter in a debate over the last three years about how to use IFC's net income; attempts to use it independently or internally through funding technical assistance and grants for output-based aid have been criticized; and now attempts to give it away to IDA have met with resistance and calls for restraint.

Multilateral Investment Guarantee Agency (MIGA)

The size of MIGA's total gross guarantee portfolio has grown from \$5.09 billion in FY05 to \$5.36 billion in FY06 with \$1.30 billion of new business and \$1.03 billion of runoff of existing portfolio.

During FY06, the diversification of MIGA's guarantee portfolio has improved, with the share of Europe and Central Asia contracts now slightly below the FY04 level and the share of financial sector contracts now below 30 percent. Close to 80 percent of FY06 contract cancellations were due to either the switch to self-insurance or the fact that underlying insured assets were no longer at risk. The overall portfolio risk, measured by the Economic Capital, has increased by about eight percent, largely driven by the growth of total net exposure.

At the June 2006 Board discussions of MIGA's three-year (FY07-09) business plan and FY07 administrative budget, the Board welcomed the Agency's progress in diversifying its guarantees portfolio. It expressed concerns regarding the need for continued realignment of the guarantee business, confronting the complex challenges of cancellations and streamlining the technical assistance programs of MIGA.

CONSTITUENCY COUNTRY DEVELOPMENTS

Australia

In April, 2006, the Australian Government launched the first-ever 'White Paper' (or government strategic policy document) on Australia's overseas aid program *Australian Aid: Promoting Growth and Stability*. The White Paper will shape the delivery of Australia's aid over the next ten years and provides a comprehensive account of how the Australian Government will approach Australia's goal of doubling its aid budget to about \$A4 billion annually by 2010.

The White Paper focuses on four areas: accelerating economic growth; fostering functioning and effective states; investing in people; and promoting regional stability and cooperation. The White Paper outlines measures to strengthen the effectiveness of Australia's aid, including an enhanced strategy to help governments in the region combat corruption. The Australian Government has stated that its aid comes with reciprocal responsibility – governments receiving aid must strengthen governance, speed reforms, and actively combat corruption to ensure that aid makes a difference.

The World Bank will be a prominent partner in implementing a number of the White Paper initiatives, particularly in the areas of infrastructure, results measurement and anti-corruption. In the latter part of FY06, a series of discussions were held with World Bank management with a view to advancing White Paper initiatives, most notably through a visit to Australia by Jeff Gutman, acting Vice President for East Asia and the Pacific.

In May, the Australian Treasurer, The Hon. Peter Costello, delivered Australia's FY06-07 budget embodying the first fiscal expression of the White Paper. The aid budget featured a 9 percent real growth in the volume of ODA, raising the Australian ODA/GNI ratio to 0.3 percent. The budget included an announcement of A\$136.2 million to fully finance up-front Australia's share of the first 10 years of the MDRI.

Australia announced support for a number of key World Bank initiatives, including \$A1 million for the Knowledge for Change program and \$A500,000 for the Social Accountability programs. Initial discussions were held with Bank staff with a view to establishing a research partnership between AusAID and the World Bank. Australia provided \$A73.2 million to IDA and \$A14.7 million for the Heavily Indebted Poor Countries Initiative in 2005.

Cambodia

The Eighth Meeting of the Consultative Group (CG) for Cambodia was held in March, 2006, in Phnom Penh. This meeting followed on the heels of the launch of the Bank's Cambodia Poverty Assessment 2006 report. Achieving the priorities laid out in the Government's new five-year National Strategic Development Plan 2006-2010 (NSDP) is critical to Cambodia's success in the fight against poverty and this was the key focus of the CG Meeting. Participants also assessed the Joint Monitoring Indicators adopted at the last CG Meeting in December 2004 and endorsed by the Government and development partners as action items on the reform agenda, and agreed upon a new set of indicators for the upcoming year. Discussions also focused on economic and

social developments, increasing aid harmonization and effectiveness, and financing requirements for development assistance.

The Bank's Poverty Assessment 2006 report found that while Cambodia has made greater progress in reducing poverty over the last decade than previously estimated, new and more complex institutional and policy changes and strengthened partnerships are needed if the country is to achieve its Millennium Development Goal of halving poverty by 2015. The Poverty Assessment presents for the first time comparable estimates of household consumption and poverty between different years in Cambodia, and identifies the key successes, lessons, innovations and remaining challenges in reducing poverty in the country. Prime Minister Hun Sen, opening the Launch of the Poverty Assessment, welcomed the new poverty figures. He reminded the audience that the robust growth underpinning poverty reduction over the last decade was based primarily on garment exports and tourism, which generated many jobs in urban areas, but had limited impact in rural areas where 91 percent of the poor live.

Currently, there are 23 Bank assisted projects with total commitments of \$257.9 million under implementation in Cambodia.

The Bank has declared mis-procurement in seven Cambodian projects and suspended disbursement in three. However, the Bank's actions were highly selective, focused on halting disbursements in only those parts of projects where problems have been identified, while maintaining disbursements elsewhere. Notwithstanding the suspensions, President Wolfowitz recommended the Board's approval of the Cambodia Public Financial Management and Accountability Project (PFMA) and the Board unanimously approved the project at the 27 June meeting.

On 29 June 2006, the Board discussed both the Inspection Panel's investigation of whether Bank management had correctly implemented Bank policies in the 2000-2005 Cambodia Forest Concession Management and Control Pilot Project, and management's response to the Inspection Panel's findings. Discussion focused on the many challenges remaining for future forest sector reform in Cambodia and better ways in which the Bank could assist. One of the main lessons learnt from the project was the importance of broad and inclusive consultations with all stakeholders before proceeding with any future projects.

Executive Director Choi and Advisor Chris Tinning visited Cambodia in mid-July 2006. The visit was important to convey to the authorities the Board's views and comments from the June meetings on Cambodia, and to solicit the authorities' views and concerns for further discussion with President Wolfowitz.

Korea

Over the past year, Korea has continued to diversify and deepen its cooperative relationship with the World Bank both in its financial and non-financial aspects.

The World Bank President, Mr. Wolfowitz, visited Korea in June 2006, accompanied by Executive Director Choi. He met the President of Korea, Moo-Hyun Roh; Deputy Prime

Minister and Minister of Finance and Economy, Duck-Soo Han; Minister of Commerce, Sye-Kyun, Chung; and Minister of Information and Communication, Jun-Hyung Roh. The visit provided an opportunity for Mr. Wolfowitz to discuss improvements in the partnership between Korean government and World Bank Group. At a seminar jointly organized by the state-run Korea Development Institute and the Korean Trade Investment Promotion Agency (KOTRA), President Wolfowitz noted that Korea is a “valuable model” for other developing countries and he emphasized the importance to extract the lessons to be learned from Korea’s success and to share them with other developing countries.

To improve the partnership, Wolfowitz and Ki-Hwan Hong, who is president of KOTRA, signed a Private Sector Liaison Officers (PSLOs) agreement. PSLOs, which other countries are already using successfully, will link the Bank with private sector firms in Korea that may want to do business with the Bank. Under the agreement, KOTRA can appoint PSLOs to the World Bank to liaise with the World Bank Group to deepen bilateral collaboration in order to achieve common objectives, promoting both trade and investment in the World Bank’s developing member countries.

The Korea Consultant Trust Fund received \$465,000 this year. The Fund was fully utilized for hiring consultants in the Bank’s operations in East Asia and Latin America. The Korean government’s contribution to the Fund totals \$5.2 million since its establishment in 1993. Korea has actively participated in the Debt Relief negotiations and pledged a contribution of SDR249 million. This accounted for 1.0 percent of total donor contributions.

Looking forward Korea intends to share its reservoir of experience and thereby assume a role, however modest, in the socio-economic advancement of developing nations and take an active part in international efforts to promote our common prosperity. Korea is trying to assume responsibilities and roles along a broad spectrum of areas that would befit a nation of Korea’s economic size and capacity.

Korean President, Roh Moo-Hyun, announced on his trip to Sub Saharan Africa in March 2006, that the Korean Government plans to triple its official development assistance (ODA) to Africa over the next three years, expanding aid in the fields of medicine, health services, information technology and the development of human resources. In addition, Korea plans to double its total overseas development assistance from 0.06 percent of GDP to 0.1 percent of GDP by 2009. Korea will establish two trust funds totalling \$30 million, with the World Bank. One is to support the development of activities in the area of information and communication technology. The other would be support a broader range of poverty reduction and socio-economic development activities across a number of sectors. In addition Korea will also establish a \$2 million trust fund with IFC.

Mongolia

Representatives of external partners and the Government of Mongolia (GoM), attended a technical meeting, jointly organized by the Government of Mongolia and the World Bank. The meeting was held in Ulaanbaatar in late February and early March 2006. The objective of the technical meeting was to exchange views between the Government and external partners on

Mongolia's development program for the coming 12-24 months, with a special focus on development financing, private sector, education and harmonization. The technical meeting marks a shift in the Government-external partner cooperation to better align external support with the government's own planning and budget cycle through regular six-monthly meetings focused on improving the management of development results.

The government and partners agreed on new mechanism of cooperation based on the principles of accountability, transparency, support of real economic development, results on the ground and elimination of any overlaps. To generate a needs-based programmes of activities costs and aligned within sustainable resource envelopes, the government and partners also agreed on the need to strengthen capacity and institutions to make sure the national strategy, medium-term planning, and the budget process are strongly linked.

At the technical meeting, Minister of Finance N. Bayartsaikhan noted the need to increase the efficiency of foreign loans and aid, while bearing in mind the current high level of external debt, numerous competing needs, and vulnerability to external conditions. David Dollar, World Bank Country Director for Mongolia emphasized the need for prioritization at both the macro and micro levels.

Three IDA projects totalling \$26 million in grants were approved by the Bank Board in FY06: Governance Assistance; Rural Education and Development; and Information and Communication Infrastructure Development. The Governance Assistance project will assist the government of Mongolia in improving the efficiency and effectiveness of governance, promoting transparency and accountability in the performance of public sector functions, and in improving the investment climate. The Information and Communication Infrastructure Development project will increase the coverage and use of relevant information communication technology (ICT) services among the rural population through an incentive programs designed to encourage private operators to provide their services in the rural segment of the ICT market; and to increase private sector participation in the delivery of e-government services, thereby improving public sector utilization of ICT. The Rural Education and Development project grant will assist Mongolia in enhancing the quality of education in rural primary schools, grades 1-5, by improving students' access to, and use of, quality learning materials and improving teachers' skills through promoting professional networks.

There are currently nine Bank assisted lending projects with total IDA commitments of \$136.5 million and three grant projects with total commitments of \$26 million under implementation in Mongolia. Disbursements for lending projects were low at 13.2 percent in FY06 compared to 30.1 percent in FY05. Grant projects performed relatively better with disbursements at 30.5 percent.

Our office visited Mongolia in early June 2006. During the visit, Executive Director Choi met with high ranking government officials and discussed the country's development issues.

New Zealand

New Zealand welcomed and joined the Multilateral Debt Relief Initiative. NZAID is contributing a total of some NZ\$68 million to this initiative.

Annual high level consultations between NZAID and the WB Sydney office, the focal point for World Bank operations in the Pacific, have now become a regular feature of calendar. This consolidates a partnership that was already noteworthy for its strength and effectiveness. In addition, New Zealand continued its strong commitment and support to IFC regional sub-units, the Pacific Enterprise Partnership (formerly the Pacific Enterprise Development Facility), and the Mekong Project Development Facility.

NZAID's Jakarta-based and Wellington staff continue to engage with IFC in Indonesia. It also supports the current Foreign Investment Advisory Service's Pacific operations from its Asia-Pacific office in Sydney. Efforts to build greater coordination between the Private Sector Development activities of the World Bank Group in the Sydney office are welcome.

New Zealand has welcomed the World Bank's contribution to understanding current issues in the Pacific. Over the past year, this has included research on Pacific migration and remittance flows, a report on natural hazards management and the Pacific Infrastructure Report. These provide a solid underpinning for policy decisions, developing country and regional strategies and for programming.

New Zealand is also supporting the application in the Pacific of the World Bank's flagship global initiative on the *Costs of Doing Business*. This includes support for the implementation of the related decisions of the Pacific Islands Forum Economic Ministers Meeting in 2005 through FIAS in conjunction with the rest of the IFC and World Bank Group.

NZAID is supporting the multi donor trust fund for Aceh (\$8 million over four years) and the Consolidated Budget Support (\$3 million over three years) programs in Timor Leste coordinated by the World Bank. NZAID is finalising a contribution of \$200,000 to support the Bank's implementation of the Lao PDR Harmonisation Action Plan. NZAID is fully engaged in discussions to develop the Public Expenditure and Financial Accountability framework (PEFA) an analytical tool provides an opportunity for furthering the harmonization agenda in the Pacific region.

NZAID is now contributing (NZ\$750,000 in 2005/06) to the Pacific Facility 3, joining the World Bank and AusAID in this initiative by the Bank to extend technical assistance to Pacific Island countries independent of lending operations and through a mechanism that can react more quickly and flexibly to needs within the region than those traditionally available through multilateral development banks.

At the bilateral level, the past year has seen initiatives for deepening cooperation between the World Bank and NZAID over a range of sectors and PDMCs, including the development of a health SWAP in Samoa, an education SWAP in the Solomon Islands (preceded by a co-financed national skills survey), cooperation on a rural livelihoods program, also in the Solomon Islands

and exploring opportunities for collaboration in Vanuatu in the areas of private sector and rural sector development.

On his appointment by President Wolfowitz to one of the Bank's two MD positions, Graeme Wheeler became the first New Zealander to be appointed to a WB top management position.

On 6 September 2005, New Zealand started the process of becoming a member of MIGA by signing the MIGA Convention at a small signing ceremony held at the Bank. The Convention was signed on behalf of the New Zealand Government by Ambassador, H.E. John Wood.

Pacific Member Countries

The report *'Doing Business 2006, Creating Jobs'*, included data on all of the Pacific member countries in our constituency. This report, the third in a series of annual reports that examines member countries' business regulations, remains a useful analytical work and reference for the Pacific member countries in improving their business climate. Our office has continued to encourage annual inclusion of all of our constituent countries and has worked with Bank management to ensure that the country-level assessments undertaken are thoroughly done.

With the international community becoming highly conscious of the multi-billion dollar costs of disaster relief and rehabilitation, the Bank has moved to enhance efforts in risk mitigation to make disaster relief and rehabilitation more cost-effective. The Pacific member countries rank among the most vulnerable in the world to natural disasters with the costs of natural disasters in the 1990's amounting to \$2.8 billion (real 2004 equivalent).

In 2006 the Bank commissioned a Policy Note entitled *"Not if but When - Adapting to Natural Hazards in the Pacific Islands Region"*. The Note encourages donors and recipient Pacific governments to adopt a more affordable risk management approach by addressing and providing for the necessary incentives, institutions and instruments for risk management of natural hazards.

The Bank has begun the process of developing insurance plans indexed to the intensity of hurricanes, droughts and earthquakes for developing countries prone to such catastrophes. Index-based insurance will pay claims based on the intensity of a catastrophe in a specific place over a specified period of time. Unlike conventional insurance, this type of disaster insurance will be less expensive and disburse claim payments quicker as they will not require estimates of losses. With the Pacific and Caribbean member countries in mind, the Bank tabled a Concept Note *"Small States Catastrophe Risk Insurance Facility"* at the September 2005 Small States Forum. Substantial work is underway by Bank management to put the Facility in place and allow small states, including the Pacific member countries, after successful piloting of the Facility in the Caribbean countries, to buy parametric insurance coverage against natural disaster risk. Bank staff will report on the progress of the initiative to the authorities during the 2006 Small States Forum in Singapore.

During FY06, the Bank completed its study of demographic and migration factors in the Pacific. The report, titled *"At Home & Away: Expanding Job Opportunities for Pacific Islanders through Labour Mobility"*, was published in August 2006. The report advocates greater mobility for

Pacific Strategy Monitoring Table

Constituency Member	Project	Operation type and Non PF3 Contributions Est. \$
A. Strengthening Government Capabilities in Service Delivery		
1. Improving the Effectiveness of Public Expenditures – Social Sectors		
Samoa	Health SWAP (with NZAID) Health Sector Management	Lending. IDA \$3-6m; NZAID TBC. FY08 IDA \$5.0m Supervision
Solomon Islands	Health Sector Development Health SWAP (with AusAID) National Development Plan Education Skills Survey (with NZAID, EC)	IDA \$4.4m IDA (grant) \$3-4m; AusAID FY07 AAA AAA
Vanuatu	Education Sector Strategy (with AusAID, NZAID, EC). Preparation for SWAP.	AAA
Regional	<ul style="list-style-type: none"> • Pacific Fast Track Initiative (Education For All) • Human Development Review of Health, Education and Social Protection in the Pacific. • Financial Management Harmonization (PEFA) • Procurement Harmonization 	AAA AAA AAA AAA. Focus on Samoa, Solomons
2. Improving the Management of Infrastructural Assets		
Samoa	Infrastructure Asset Management programs Phase 3 Infrastructure Asset Management programs Phase 2	Lending IDA \$6-9m. FY07 IDA \$10m
Regional	Pacific Islands Infrastructure Review	AAA (w ADB, AusAID, NZAID)
3. Safeguarding Service Delivery by Improving Resilience to natural Hazards		
Kiribati	Kiribati Adaptation programmes	GEF \$4m, AusAID \$1m, NZAID \$1m
Samoa	Cyclone Emergency Recovery programs	Lending IDA \$3m
Regional	Risk Management and Adaptation - Natural Hazard Management Policy Note & Follow-up	AAA
B. Improving Incentives for Private Sector-Led Growth and Employment		
1. Facilitating domestic job Creation through reductions in the regulatory and administrative barriers to business development and improving service and cost in Utilities		
Palau	Oil Sector Assistance	ROC \$200k, Denmark \$200k To establish new trust fund.
Samoa	Telecommunications and Postal Reform	Lending IDA \$4m
Solomon Islands	Renewable Energy Project Telecommunications Reform Power and Water Utility Reform	Lending. Req. to PPIAF \$280k IDA (grant) \$4.0m. FY08 AAA AAA
Vanuatu	Utilities Reform - Contract Management Unit Capacity Building	AAA
Regional	Private Sector Development Reform with FIAS, PEDF Telecommunications Reform	AAA AAA
2. Increasing sustainable revenues from resource-based sectors, such as fisheries or tourism		
Solomon Islands	Rural Development Project Rural Sector Strategy	Lending IDA (grant) \$0.1 m; AusAid; EC AAA
3. Improving access to regional labour markets		
Regional	Pacific Islands Migration Study	AAA

unskilled workers from the Pacific Islands to help overcome the challenges the region faces because of small economies, remoteness, growing youth populations and low job growth. The report provides a valuable framework to Pacific countries for the development of a migration policy.

The Bank has been exploring with the Republic of Malta an offer to establish a network aimed at improving knowledge and promoting good economic development policies in small states. Small states authorities will be briefed on the proposed initiative during the Small States Forum in Singapore.

Following the FY05 Board endorsement of the *Pacific Regional Engagement Framework FY06-09*, a series of country-specific and regional lending, grant and advisory activities have been initiated. These newly planned projects will be submitted for Board approval and are centred on two pillars of the Bank's framework; strengthening government capabilities in service delivery and improving incentives for private sector development. Consistent with recommendations from the Bank's evaluation of its earlier operations in the Pacific, the support comes in the form of analytic and advisory work, collaboration with donors and financial support in the form of loans and grants.

In FY06 our office visited all Pacific member countries with exception of Kiribati as part of the consultation process. The Executive Director, Choi and Rhinehart Silas (Advisor) travelled to Palau and the Solomon Islands. Terry O'Brien (Alternate Executive Director) travelled to Vanuatu. Joanna Gordon (Senior Advisor) travelled to Marshall Islands. Chris Tinning (Advisor) visited Federated States of Micronesia (FSM). Lucas Alkan (Advisor) visited Samoa. A plan to visit Kiribati had to be postponed because of airline disruption and will be rescheduled for FY07.

Papua New Guinea

The PNG Government, with assistance from the World Bank, is continuing to implement the recommendations from the Public Expenditure Review and Rationalization Project (PERR). The PERR identified a number of possible improvements for PNG's institutions and systems and set out a process by which those reforms could be progressively addressed. The review has PNG ownership and a coordinated approach has been adopted to take the recommendations forward. PNG has made considerable progress since mid 2004 in implementing key areas of the recommendations including: restoring fiscal discipline; reducing the size of civil service payroll; restoring the integrity of budget institutions and systems; and expenditure adjustment and prioritization. The government in conjunction with AusAID, is continuing to implement other areas of reform as recommended by the PERR report.

Initial rounds of discussions with the PNG on the preparation of a new CAS were held early this year. The WB country manager, in conjunction with PNG authorities is currently carrying out consultations among stakeholders for the preparation of a full Country Assistance Strategy to be ready by early next year. The CAS will replace the current Interim Strategy that was introduced in April 2005 and is due to expire in December 2006.

Critical to success of the Bank's CAS will be substantial dialogue with the government on the development agenda to be supported by the Bank during the 2007-2010 period. In the CAS, the Bank is anticipated to spell out the expected scale and scope of support for PNG. Authorities have requested the Bank to assist in impact projects such as road infrastructure and productive economic sectors as outlined in the country's MTDS.

In March 2006, Lucas Alkan (Advisor) visited Papua New Guinea as part of the constituency consultation process. He had meetings with PNG authorities including officials in the ministries of Treasury and Finance and Planning. Discussions focused on PNG's current relations with World Bank and possible steps to enhance the relationship. The PNG authorities indicated that the Bank is an important development partner and should remain engaged. They requested the Bank to come up with a full CAS as soon as possible; taking into account the government's published documents including the MTDS, Debt Sustainability Strategy and the Medium Term Budget Framework (MTBF).

There are currently five Bank assisted projects under implementation in PNG. However, it is an aging portfolio with three of the five projects expected to close at the end of this year and a fourth in 2007. Projects in the pipeline are very thin (smallholder agriculture development project and the roads maintenance and rehabilitation project which is under discussion).

IFC's contribution to the PNG Microfinance Project that was approved by the IFC Board in June 2005 is progressing well with substantial private sector equity participation.

ANNEX 1 CONSTITUENCY OFFICE**a) Strategic Goals**

We seek to advance the interests of the members of the *constituency* by pursuing the following strategic objectives:

- (a) Ensuring that the Bank hears the voice and understands the interests of our constituency in its policy development and operational decisions;
 - (b) Advocating policies (including the promotion of economic growth as a key means of reducing poverty) and implementation practices that improve the effectiveness and efficiency of the Bank;
 - (c) Encouraging the Bank to engage actively with our constituency members, in particular Cambodia, Mongolia, Papua New Guinea and the Pacific Islands;
 - (d) Encouraging our constituency members to engage actively with the Bank. To this end, we work to increase the understanding among constituency members of the Bank's policies and activities;
 - (e) Assisting co-ordination between the development-assistance programs of the Bank and donors (in particular, Australia, Korea and New Zealand) to the developing-country members of our constituency; and
 - (f) Facilitating contacts between businesses in constituency countries and the Bank, including consultancy and procurement contracts.
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b) 2005-2006 CONSTITUENCY OFFICE - STAFF**EXECUTIVE DIRECTOR**

Mr. Joon-Kyung Choi Korea Elected: 1 August 2005

ALTERNATE EXECUTIVE DIRECTOR

Mr. Terry O'Brien Australia Appointed: 23 July 2003

SENIOR ADVISORS

Mr. Kyu-Yun Choi Korea Appointed: 15 September 2004

Ms. Joanna Gordon New Zealand Appointed: 25 July 2005

Ms. Damba Baasankhuu Mongolia Appointed: 1 March 2006

ADVISORS

Mr. Lucas Alkan Papua New Guinea Appointed: 22 November 2004

Mr. Rhinehart Silas Palau Appointed: 29 November 2004

Mr. Chris Tinning Australia Appointed: 12 September 2005

Mr. Yoon Kyung Kim Korea 3 February 2003 – 13 Feb 2006

OFFICE SUPPORT STAFF

Mrs. Yolanda Cunnane Senior Executive Assistant

Mrs. Hille Blackshaw Staff Assistant

Mrs. Elena Chanchu Staff Assistant

c) CONSTITUENCY OFFICE TRAVEL: 1 JULY 2005 – 31 JULY 31 2006**1. Joong Kyung Choi , Executive Director**

11-23 November 2005	Koror, Palau; Honiara, Solomon Islands, CWA; Sydney, Australia, WB Office
11-26 January 2006	St. Petersburg, Russia, ABCDE Conference; Seoul, Korea, CWA
4-9 April 2006	London, England, LSE Conference
28 May-9 June 2006	Tokyo, Japan, ABCDE Conference; Seoul, Korea, accompanying Mr. Wolfowitz; Ulaanbaatar, Mongolia, CWA; Beijing, China, Consult with WB Staff
10-15 July 2006	Phnom Penh , Cambodia, CWA

2. Terry O'Brien, Alternate Executive Director

9-11 September 2005	Paris, France, DC Deputies and IDA14 Meeting
4-11 October 2005	Canberra, Melbourne and Sydney, Australia, CWA
28 January-26 February 2006	Sydney, Australia; Port Vila, Vanuatu, CWA
4-12 April 2006	Paris, France, DC Deputies Meeting

3. Damba Baasankhuu, Senior Advisor

28 May-8 June 2006	Ulaanbaatar, Mongolia, CWA, with ED
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4. Joanna Gordon, Senior Advisor

9-12 September 2005	Paris, France, DC Deputies and IDA14 Meeting
22 January-12 February 2006	Majuro, Marshall Islands; Wellington, New Zealand, CWA

5. Lucas Alkan, Advisor

4-21 March 2006	Apia, Samoa; Port Moresby, Papua New Guinea, CWA
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6. Rhinehart Silas, Advisor

11-23 November 2005	Koror, Palau; Honiara, Solomon Islands; CWA; Sydney, Australia, WB Office, with ED
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7. Chris Tinning, Advisor

26 February-12 March 2006	Pohnpei, Federated States of Micronesia; Canberra, Australia, CWA
10-15 July 2006	Phnom Penh, Cambodia, CWA, with ED

8. Yoon-Kyung Kim, Advisor

September 9-12 2005	Paris, France, DC Deputies and IDA14 Meeting
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CWA – Consultations With Authorities

ANNEX 2 CONSTITUENCY STATEMENTS**a) STATEMENT BY THE HON. DUCK-SOO HAN, DEPUTY PRIME MINISTER AND
MINISTER OF FINANCE AND ECONOMY, REP. OF KOREA
Development Committee Meeting, September 25, 2005**

Since the April 2005 meeting of the Development Committee, developing countries have continued to grow at about twice the rate of high-income countries and sub-Saharan Africa is continuing its welcome acceleration of growth. There are, however, wide disparities between developing countries. Following strong growth in 2004, the global economy during 2005 has exhibited more moderate growth, while inflationary pressures remain subdued. However, the downside risks are increasing with wide growth divergences and increasing global imbalances, against a background of record-high oil prices and gradually rising short-term interest rates. At the moment when we want to accelerate progress against poverty, the global growth environment may become less helpful. This should encourage us to think again about how to increase and sustain growth in the developing world.

One-third way towards 2015: a sense of urgency

Since leaders endorsed the millennium development goal (MDGs) in 2000, the world is now one-third of the way towards the target date of 2015. The MDG of halving poverty is likely to be met at the global level, but goals for gender outcomes in education, and for improved maternal and child health are likely to be missed in many regions. Most MDGs may be missed in most of Africa, notwithstanding the strong per capita income growth in reforming economies such as Benin, Burkina Faso, Cameroon, Ghana, Mozambique, Rwanda, Senegal, Tanzania and Uganda.

We must redouble our efforts to reform policies and institutions, improve governance, open up trade opportunities and improve aid flows and debt management. Only higher sustainable economic growth in developing countries can accelerate progress towards the MDGs. Because of the compounding nature of growth, any step-up in sustainable growth countries can achieve early in the remaining 10 years to 2015 will achieve much more poverty alleviation than a similar increase closer to 2015.

Strengthening the development partnership for achieving the MDGs***Aid effectiveness***

Real growth in ODA has approached 5 percent per annum in the last few years, and there have been recent pledges of some 60percent real growth over the next 5 years. If the G-8 proposal for debt forgiveness is implemented, some \$40 billion (depending on final decisions on details) that would have gone in debt repayment by heavily indebted poor countries will instead be left with HIPC governments (especially in Africa). These are very large financial resource increases that will constitute large portions of government budgets and GDP in many of the poorest countries.

Managing and absorbing such financial increases will require careful management and coordination to ensure they do not trigger price increases, real exchange rate appreciation and loss of competitiveness in the tradeable sectors of the economy (so-called 'Dutch disease'), and undesirable declines in governments' revenue self-reliance and accountability to their citizens. It is apparent from research into experience over the last 40 years that these adverse consequences of heavy reliance on aid too often detracted from the ability of ODA to cause a sustained increase in the rate economic growth.

We therefore welcome progress towards implementation of the 12 indicators suggested in the *Paris*

Declaration on Aid Effectiveness, which will improve recipients' financial management and procurement systems, better align aid to recipient priorities, better coordinate donor effort (including in analytical work) and improve aid predictability. Signatories to the declaration in this constituency pledge to work to achieve its targets, and are already applying its principles. We endorse the findings of the *Review of World Bank Conditionality*, and encourage the implementation of the improved practices it outlines. Progress requires that the streamlining of conditionality should not now lead to an increase in 'triggers' which may undo the benefits of streamlining. The *2005 Review of the Poverty Reduction Strategy Approach* usefully updates on this vital initiative, which can enhance country ownership and accountability, and help facilitate donor coordination.

The *Infrastructure Progress Report* shows improvement of the World Bank's performance in this vital area, and it is pleasing that increased volumes of lending have been achieved while maintaining good project quality. Further improvements will be vital, as carefully-selected infrastructure investments not only improve productivity, but can be part of a strategy to minimize 'Dutch disease' through lowering the costs of the traded goods sector, and moderating upward exchange rate pressure through the import content of infrastructure projects, which is often higher than for social projects.

New financing initiatives

We are interested in the exploratory work on Advance Market Commitments for new vaccines.

As notified at earlier Development Committee meetings, our donor economies do not wish to participate in any IFF-type mechanism at this time. Nor do we see any attractions in various international taxation options, which we regard as having problems of accountability to taxpayers, and of governance.

We note the preliminary study of additional international aviation taxes. We are concerned that additional aviation taxes would hinder tourism and trade. An international aviation tax could threaten the survival of some airlines in a very competitive industry, currently facing high fuel costs. For the small and remote economies represented in this constituency who seek to develop their tourism industries, airlines taxes would be very undesirable. In our view, aviation tax proposals do not have sufficient support to warrant further work by the Bank or Fund.

G-8 debt relief proposals

The *Heavily Indebted Poor Countries (HIPC) Status of Implementation Report* shows welcome progress since the last report in September 2004 in the take-up of the HIPC scheme, with 28 countries now having reached the decision point, of which 18 have gone on to reach the completion point. But examination under the newly-agreed Debt Sustainability Framework of those countries that have reached completion point and received enhanced HIPC treatment, suggests they still have large debt stocks.

Consequently, we support the broad principles of the June 2005 G-8 proposals for 100percent forgiveness of loans from the International Development Association, the IMF and the African Development Fund to HIPCs successfully reaching completion point. For the proposal to deliver its benefits, we consider it is essential for the countries concerned to allocate the resources freed from debt servicing to poverty reduction, and for donors to supply funds to IDA to make good the foregone reflows from HIPCs, additional to existing ODA commitments. We especially welcome the G-8 proposal that those additional funds should be allocated on the basis of performance across all IDA-only developing countries.

It will be vital to monitor the operation of future lending from all sources to avoid the re-accumulation of unsustainable debt in the HIPC's, and to ensure equitable access to IDA finance for both former HIPC's and others. Accordingly, we welcome the timely review next year of the Debt Sustainability Framework.

We urge endorsement of the G-8 proposal, and the prompt finalisation of important financial, legal, accounting and auditing details that are necessary to put the proposals into effect through all three institutions. Our IDA donor members are prepared to pay their share of the G-8 proposal's costs to IDA.

Africa Action Plan

We welcome the formulation of the Bank Group's *Africa Action Plan*, with its emphasis on a results framework for specifying, measuring and managing to achieve specified outcomes, and its efforts to strengthening the private sector drivers of growth. While we wholeheartedly wish the successful implementation of the Africa Action Plan, we note that the challenge now will be to convert the 25 proposed priority actions for the region into sensible action at the level of the 47 very diverse countries of sub-Saharan Africa.

We suggest several World Bank Group priorities for action to assist those African countries most at risk of missing most of the MDGs. First, the plan must address the distinctive challenge of Africa: the higher prevalence than in any other region of fragile states. The Bank's Low Income Countries Under Stress (LICUS) initiative has sought to establish new ways of working with such fragile states, including the important sub-set of post-conflict states. We urge that the LICUS initiative should now be properly financed and placed centrally in the Bank's work in all fragile states. There will be some instances where political failure will preclude Bank involvement by any means, but properly resourced work with LICUS approaches should allow improved performance in many other fragile states.

LICUS or fragile states in Africa and elsewhere suffer such intractable and chronically weak governance that the ir development challenges can not be addressed through the IDA performance-based aid approach. We would be supportive of focused Bank work to find new ways of appropriately financing and staffing Bank engagement with LICUS. We consider that exploration of new ways should look to the LICUS challenge globally.

We believe, more fundamentally, that with launching the Africa Action Plan, African countries themselves should scale up their efforts to improve governance, transparency and accountability. Without self-effort to change the old systems, no external assistance can bear fruit. "*Doing business in 2006: Creating Jobs*", shows some success stories in this regard. Rwanda, among others, has achieved the highest level of economic growth in the region since it made it easier to start business by reforming its regulations.

The Doha Development Agenda and 'aid for trade'

Doha and real resource transfer to development countries

The Development Committee is the "Governors of the Bank and the Fund concerned with the transfer of real resources to developing countries". Trade is a principal means by which the financial resources from aid and debt relief are converted into the real resources that combat HIV/AIDS and malaria, that build infrastructure, and globally competitive and productive industries in the formal economy. It is those formal-sector industries and their employees, which pay taxes and allow governments to deliver vital services.

Increased ODA and debt forgiveness are being implemented quickly. But it takes time to convert those financial resources into real resources through creating, formal-sector businesses and gaining world markets for exports from developing countries. To reduce that lag, we need a comparable sense of urgency in achieving the Doha Development Agenda as has driven the commitment of increased aid and debt forgiveness.

If we substantially increase the financial resources to developing countries but do not increase the trade opportunities for them to increase their real resources, we risk much worse than wasting aid. We risk worsening the uncompetitiveness of the formal sectors in developing countries, inflicting the worst damage on the weakest economies receiving the most aid and debt forgiveness.

Because of these concerns, we agree with the proposals of the *Trade Progress Report*: Rich countries must make ambitious market openings in agriculture; and poor countries and middle income countries must also participate.

When developing countries lower their own trade barriers, their access to lower cost imports obviously increase their inflow of real resources. But sustainably paying for those imports requires export growth, which is facilitated by reducing protection in others' markets. Just as importantly, openness to trade helps development by raising productivity. It improves competition, reduces corruption and rent seeking, lowers input costs to business even outside the tradeable sector, and improves the capacity of local business.

Aid for trade

Behind a successful trade round, 'aid for trade' offers improved supply-side opportunities for developing countries to realize new trade opportunities. We warmly support the *Trade Progress Report's* proposals to enhance aid for trade, and note the proposed expansion of a reformed Integrated Framework of Trade-Related Technical Assistance. We note the governance problems which have hindered the past effectiveness of the Integrated Framework, and emphasise that correcting those problems is an important step to greater effectiveness, which also requires more focus on outcomes, expanded country coverage, better targeting and timeliness, and more responsiveness to partner needs. We support the Bank continuing its useful trade-related assistance under the Pacific Enterprise Development Facility.

Expanding trade is closely related to expanding the formal sector of the economy, and in this context we again stress the potential of *Doing Business in 2006: Creating Jobs* to lower the 'behind the border' barriers to trade. The previous edition of *Doing Business* included all our constituency members in its database for the first time. The June 2005 meeting of the Pacific Island Forum Economic Ministers in Tuvalu committed the Forum states to work towards halving, by FEMM 2007, the time it takes to start a business, the cost of registration, the time to go through insolvency and the cost of enforcing contracts. This is an example of how good analytical work by the Bank can inform and motivate reforms 'behind the border' in a way that can improve business climate, and strengthen capacity to trade.

Climate Change and the World Bank Group

We welcome the short background paper *Climate Change, Energy and the World Bank*, and the actions it details for the Bank to take up a facilitating role for developing clean energy and sustainable development, in response to the requests from the G-8. While the Bank must remain focused on poverty alleviation, we respect the expertise it has built on sustainable development, carbon markets, and ways to ensure developing countries can both enjoy economic growth and facilitate environmental protection in

ways that are mutually advantageous to all.

In that context, we would encourage the Bank's engagement with the Asia Pacific Partnership on Clean Development and Climate. This is collaboration between Australia, China, India, Japan, the Republic of Korea and the United States, to address energy, climate change and air pollution issues within a paradigm of economic development. These partners together account for about half of the world's GDP, population, energy use and greenhouse gas emissions. The Partnership focuses on practical action to develop and deploy low-emissions technologies which complement economic development and energy security goals. It will not set arbitrary targets and will focus on developing and deploying new technologies that will put economies on low-emissions trajectories.

Voice and Participation

There has been some progress within the Bank Group in enhancing the voice and participation of developing and transition economies since we last met. In particular, the secondment arrangements to give representatives of developing and transition economies greater exposure to the work and governance of the Bank have been put in place, with the first two rounds of candidates selected and moving through the scheme. We know from our constituency's involvement in the scheme that it is appreciated, and that it builds capacity in member governments to understand and influence the Bank.

However the deeper structural challenges to properly reflecting the influence of fast-growing economies await resolution. IMF work on quota review remains crucial in our view to the legitimacy and influence of the Bretton Woods institutions. We urge its speedy completion.

b) STATEMENT BY MR. TAE-SHIN KWON, VICE MINISTER, MINISTRY OF FINANCE AND ECONOMY, REP. OF KOREA**Development Committee Meeting, April 23, 2006**

We welcome Alberto Carrasquilla as the new Chair of the Joint Ministerial Committee of the Boards of Governors of the Bank and the Fund on the Transfer of Real Resources to Developing Countries, and promise our support for improving the effectiveness of the Spring and Annual Meetings of the DC in the governance of the World Bank Group and the IMF.

We would like to see the Development Committee progress as means of providing effective ministerial guidance to management on core strategic topics of more effective operation, governance and reform of the Bretton Woods institutions – an issue to which we return at the conclusion of this statement.

Developing Country Growth continues robustly

Developing countries' GNP growth continued remarkably strongly last year, at over 5percent for the third consecutive year, once again significantly faster than developed countries' growth. If through continued reforms the developing world can sustain the growth rates of the last three years for the next nine years, its economies would be some 60percent larger in 2015 than today.

Nevertheless and sadly, it remains true on evidence in the 2006 *Global Monitoring Report*, as in previous reports, that many developing countries will not achieve the income or social Millennium Development Goals (MDGs) expressed at the country level. Again as in previous years, the shortfall looks likely to be particularly marked in Sub-Saharan Africa because of the weak starting points and relatively slow reform for many and regional conflicts hindering some. Sub-Saharan Africa has more of the world's 35 fragile states than any other region, followed by East Asia and the Pacific.

At times, the *Global Monitoring Report's* global and regional aggregation and its emphasis on Africa as a continent, means that the operational, practical lessons for the Bank's engagement in the individual countries of the various continents and regions are somewhat submerged. In every region, the weakest national performances towards the MDGs are among the 35 fragile states. Fragile states account for one-third of the world's poor; one-half of children dying before 5; over one-third of maternal deaths; and over one-third of people with HIV AIDS

But understandably, because of their generally weak governance and invariably low absorptive and administrative capacities, fragile states receive only one-quarter of total global aid.

If we are to accelerate progress towards the MDGs, we have to directly address the challenge of engaging more effectively in fragile states. Pleas for ever-more aid at the global level, or more effective aid, or more predictable aid, or even better harmonized aid - all undoubtedly necessary - will not take fragile states very far, when the core of their aid problem is that they cannot use traditional aid effectively. The closer we drift to 2015 without addressing this problem seriously, the less time we have to help initiate progress in those fragile states furthest from the MDGs. The Bank has the strategy to help those states; now it is time to implement it fully and with meaningful resourcing.

Setting aside the special difficulties facing fragile states, we are heartened by the spread in 2005 of strong growth to more developing countries, and signs that in many countries, that growth is pro-poor and beneficial to progress towards the education and health MDGs, not just income growth. In 2005, Sub-Saharan Africa grew as fast as the average growth of the rest of the developing world minus India and China.

More remarkably, the spread of strong growth throughout the developing world continued in the face of very high oil prices, in contrast with past oil price shocks which took a heavy toll on the developing world's economies.

We agree with the *Global Monitoring Report's* explanation of this extraordinary performance: developing countries have strengthened macroeconomic policy settings and are now much more engaged in the global economy through intensive trade linkages, which have permitted those who are oil importers to benefit from their own export growth and (in many cases) from high non-oil commodity prices. In East Asia and the Pacific, the export revenues of oil importers as a share of their nominal GDP has almost tripled from 1980 to 2005, and has now reached an average of almost 45 percent of GDP (although of course many smaller states and fragile states in the region have not strengthened their positions).

We are concerned that the Bank is not yet delivering its best in financial sector development. We consider that the Bank should focus on consolidating and managing its experience and expertise in these areas and more generally, to focus on areas where it has the comparative advantage. One of the lessons of the 1990s is that it is important also to look at 'growth diagnostics' that enable productive sectors to achieve sustained economic growth.

Of course, this year as always, there are risks to the continuation of recent growth rates: high oil prices, current account imbalances, the possible recrudescence of inflation, or the possible mutation to humans of avian flu, to name but four.

However the lessons are clear: to sustain or accelerate recent progress towards the MDGs, we will need to ensure that the trade liberalization that has engendered such resilient performance is continued. In this regard we remain committed to an ambitious and comprehensive outcome in the WTO Doha Round, one that truly delivers on the promise of the Doha Development Agenda. A successful outcome should take into account the vulnerability of developing countries including measures to support countries' ability to take advantage of trading opportunities. Investments to improve access to energy, mitigate climate change and adapt to possible global warming must be made without slowing developing countries' economic growth and their progress towards the MDGs. Finally, the promised large increase in aid flows will have to be delivered more effectively and with careful regard to absorptive capacity and the risks of real exchange rate appreciation and loss of export competitiveness from large capital inflows.

Engagement in this Constituency by the World Bank Group

We welcome the International Finance Corporation's first-ever equity investment in PNG, its placement of a resident representative in Port Moresby, and its decentralization of other operational resources into the region.

The World Bank Inspection Panel also completed an inquiry into the Bank's implementation of its policies in a Forest Concession Management and Control Pilot Project in Cambodia.

Regrettably, there is little new or additional Bank activity to report elsewhere in the constituency. It seems that business as usual is largely the abiding theme, which is of concern. Many small states in this constituency receive significant bilateral grant aid, and for them, the Bank must continue to work to its strategic niche, explore financing appropriate to small states and fragile states, including blended finance for states with little further debt carrying capacity, decouple lending and TA operations, provide specific and actionable advice on request, and help build capacity in partner administrations. Bank value-added will depend on better delivery of appropriately-tailored, timely technical assistance that is relevant to the countries' highest priorities.

Development Effectiveness, Strengthening Governance and Combating Corruption

Our constituency's donor economies have pledged significant growth in aid and additional contributions to the Multilateral Debt Relief Initiative.

In order to lock in aid increases and debt relief pledged by the world's democracies, we need continued transparency about aid efforts through reporting by the Development Assistance Committee beyond the ranks of the OECD membership to include the emergent donors. As importantly, we need improvements in aid effectiveness, clearly demonstrated through published evaluations. The generous public response to some natural disasters, and the increasing role of private foundations and global program as new funding channels, suggest willingness to contribute where there are well-targeted proposals with prospects for achieving clear goals. We cannot assume that these contributions will continue, unless we can deliver credible results in return.

While positive in terms of raising funds, global program present a challenge, most clearly apparent in the area of health: how do we ensure that country development priorities are respected and local delivery systems are not undermined? We would appreciate continuing Bank work on this challenge.

Avoiding another 'lend and forgive' cycle

The Multilateral Debt Relief Initiative provides some US\$50 billion in resources, effectively as general budget support to the beneficiary economies. Using it wisely will require well-focused, country-owned policies to create sustainable economic growth and growing exports from a vibrant private sector. Sound management by developing countries also will be assisted by better Bank work to improve fiscal and debt management systems, which independent evaluation has shown to have deteriorated in quality in the Heavily Indebted Poor Countries over the course of the HIPC initiative. Deployment of the Fund-Bank Debt Sustainability Framework will also be vital, as will the Bank's continuing work on fiscal space, and addressing the problem of 'free-riding' through achieving better transparency and cooperation among public and private lenders.

We welcome the progress report to this meeting on fiscal space and hope that completion will elaborate developing countries' options to improve their fiscal space for high priority investments. Findings will need to be applied in a country-specific way to identify and remove their most binding constraints in revenue raising, expenditure prioritization and efficiency, and managing aid flows and borrowings.

In our members' experience, we would advocate close practical attention to managing borrowing and indebtedness conservatively; history shows countries frequently have underestimated the perils of high indebtedness, and have wrongly favoured borrowing over developing their own revenue-raising capacity and prioritizing their spending. We urge the Bank to guard against over-optimism when projecting forward rates of growth or debt carrying capacity as part of debt sustainability analysis exercises.

Effective, targeted and coordinated aid

Donors will properly have their own geographical and historical priorities for bilateral aid, and recipient economies' strengths in governance and country systems should determine which forms of aid will be most effective. The multilateral development banks' share of total aid effort rests ultimately on their demonstrated effectiveness in use of their large endowments of aid.

Our donor authorities continue to work closely with counterparts in the spirit of the *Paris Declaration on Aid Effectiveness* to achieve better simplification of aid process, better use of recipient country systems where appropriate, and better harmonization among donors.

Strengthening the results focus in MDBs

Improving the performance of the multilateral development banks requires more weight on learning from transparently evaluated outcomes of aid, and motivating staff through career incentives to work in the most difficult environments in fragile states, where progress towards the MDGs has been slowest.

The Bank's strong policy framework for engaging with fragile states developed over the past few years has to date not been consistently implemented in actual country operations. Analytical and advisory work takes 16 months on average to complete, and in what are invariably subtle and difficult political situations, little attention has been paid to dissemination and implementation. A 'lending and research culture' means staff has little incentive to work on or in fragile states; 70percent of fragile states have no resident, internationally-recruited staff, or only one.

In contrast, in our constituency's bilateral aid agencies, staff work experience in fragile states commands high prestige and is a stepping stone to career advance. Research and publications are subordinate, and means to the end of effective aid delivery, not ends in themselves. The World Bank Group must build a similar work culture, rewarding achievement of development outcomes, not quantities of lending and publications.

Monitoring governance through actionable indicators

The concept of governance is broad and multi-dimensional, comprising all the ways the state acquires and exercises its authority to provide public goods and services, including regulatory services. The breadth of the concept prevents use of any single indicator. Corruption is also difficult to measure, and measurements often report perceptions as much as the country reality.

While it is important not to put too much weight on any single measure, a suite of measures can provide useful information in monitoring governance and corruption. Measurements of both concepts should be used with judgment. We would caution against integrated rankings of countries according to corruption or governance measures. We also recommend that a more operational definition of governance and corruption be introduced to help increase measurement quality. We must get this right, as governance and corruption measurement influences so much of the Bank's policy and operational work, feeding into the Country Policy and Institutional Assessment, performance-based aid allocations and debt sustainability analyses.

We tentatively agree with the *Global Monitoring Report's* identification of fourteen of the most practical, actionable governance indicators. We see special promise in extension of the Public Expenditure and Financial Accountability programs. We want to keep the Bank's monitoring effort cost-effective, operational at the country level and results-focused. We do not want our support for governance monitoring to be taken as support for another flagship publication (as past support for tracking progress towards the MDGs turned into the annual *Global Monitoring Reports*).

Even with further development of feasible indicators, decisions on how the Bank and other donors should engage with countries where governance or corruption is either improving or deteriorating rapidly will continue to require judgment, and will likely prove impossible to reduce to 'standard operating procedures'. Nonetheless, we support the President's initiative to review the Bank's experience with a view to developing guidelines.

Engaging in countries with weak governance will have to be country-specific, as we agree that even weak general governance environments will often have elements of strength and reform champions who can be assisted. Pushing reform through adding to conditionality does not work. The Bank needs to have a

strong understanding of the political economy and the drivers for change in order to know what interventions are mostly likely to succeed.

We would also advocate Bank engagement to find opportunities to improve the openness and accountability of government through improved public and international information (including use of its own Institutional Integrity processes where its own funds have been mis-spent). It should support institutions and processes that can help generate a demand for good governance, for example showing how much of budgeted spending is actually reaching local authorities for schools and hospitals, and instituting ombudsman to receive citizens' complaints.

Clean Energy for Development

Affordable access to modern energy is closely linked to human development. At present, reliance by the poor on dirty biomass fuels causes some 2 million premature deaths a year and hinders basic needs for cooking, light and heating. Inadequate power supplies limit investment, business and transport. The main 'renewable energy' in the poorest countries today is back-breaking human labour. Poor countries have urgent needs for better energy access.

Access, mitigation and adaptation challenges

Mitigation of, and adaptation to, global warming have to be development-friendly. Access, mitigation and adaptation challenges have to be solved cooperatively, and with respect for countries' individual circumstances and priorities.

Mitigation has to move beyond existing cap-and-trade approaches, which do not engage large current emitters and large fast-growing developing economies that are contributing most of the growth in emissions. Current carbon trading approaches rest on a framework whose 2012 lifespan is already crimping the cleaner use of fuels in environmentally-sound investments with long lives and payoffs, such as coal use in super-critical and ultra-supercritical thermal power plants.

Adaptation to likely global warming over decades to come is a vital challenge to many small island states such as those of this constituency, and we would urge the Bank to develop more substantial and better-funded program in this area. Neither mitigation nor (especially) adaptation is challenges only, or even mainly, for the handful of the largest developing economies.

Existing tools and proposed new financing instruments

A role for the Bank in clean energy for development requires close attention to the Bank's core mission of poverty alleviation, the vital role of the UN Framework Convention on Climate Change, and the comparative advantages of all institutions involved. In this examination, we regard evaluating the Bank's existing lending tools and processes as the paramount and most urgent challenge.

The Bank has only recently completed an overdue simplification of its array of lending products, as part of the effort to achieve more clarity in work processes and to reduce developing countries' costs of doing business with the Bank. We point also to the existing Global Environment Facility, which has elements with which several of the suggested new lending instruments would appear to overlap. Any new Bank proposals must not duplicate existing facilities, or undo the Bank's limited progress in lowering cost of doing business with the Bank.

We would also caution against premature speculation about funding a new CEFV in large part from the assumed revenues from a long-term carbon trading regime which does not yet exist.

We doubt the Bank's comparative advantage or core functions should expand to the science of climate change or of new energy technologies. However we do believe that the Bank should be mainstreaming

into its country assistance strategies the infrastructure investments to extend energy access and other energy-related assistance that countries prioritize for their own development.

We see great potential for the Bank as a development-focused partner in dialogue on climate change. In particular, the Bank is best placed to serve as a proponent for the urgent interests of developing countries in improved access to cleaner and more sustainable energy, and the particular vulnerabilities of some developing countries to inundation and other climate-driven stresses. In stressing the imperative for energy access, the Bank should drive home that reasonable growth prospects for the poor can not rest on apparently easy but illusory options using small scale renewables, but without the capacity to meet the very large energy requirements for development. Rather, these challenges will demand the Bank's serious engagement on large-scale energy options which may sometimes be unpopular with elements in rich countries.

Reform of the Bretton Woods Institutions

The IMF, the World Bank and the WTO (and its predecessors) have been core multilateral institutions for the peaceful and unprecedented rapid development of the global economy and the reduction of poverty over the last 60 years.

We believe comprehensive governance reform of the IMF and the World Bank is needed to sustain their effectiveness and legitimacy. Such reforms need to go beyond the long overdue but limited, *ad hoc* IMF quota increase being discussed for realization by the time of the Singapore Annual Meetings, to include more comprehensive quota reform which could also include consideration of an increase in basic votes. Broader governance reforms should include review of the roles and responsibilities of the Boards, and ideally, consideration of appointment processes and size of Boards.

We regard the spring and Annual Meetings of the DC and the IMFC as the apogee of the governance processes by which the Bank and Fund glean meaningful direction from Governors on a handful of *specific* issues at the frontiers of the BWIs' development.

For this meeting, we have received two fascinating publications. But as the foundation for ministerial discussions, we think those documents represent too much paper, too many diffuse questions, and not enough focus by the Bank and Fund on a manageably focused small group of practical, strategic issues for Ministerial guidance.

We urge a significantly more focused approach to these meetings in future.

ANNEX 3 WB ACTIVITIES IN THE CONSTITUENCY

a) Projects Approved by the Board in FY06

Date	\$ Million	From	Project Description
CAMBODIA			
29/06/06	\$14.0m Grant	IDA	Public Financial Management and Accountability Project The project will support Cambodia's Public Financial Management Reform program which presents a detailed, prioritized and sequenced action plan for public finance reform. The program will reduce fiduciary risk and make the budget more credible as an instrument strategic and operational management of public resources by ensuring that it delivers resources reliably and predictably to managers in line ministries.
KIRIBATI			
30/05/06	1.80m Grant	GEF	Adaptation Project – Implementation Phase II The overall objectives of this project are to develop and demonstrate the systematic diagnosis of climate-related problems and the design of cost-effective adaptation measures and to continue the integration of climate risk awareness and responsiveness into economic and operational planning. The project would also be a learning experience for other Pacific Island countries. The project will assist Kiribati in enhancing its capacity to both plan and implement measures which will reduce the detrimental impacts of climate change on the fragile atoll ecosystems in Kiribati.
MONGOLIA			
23/05/06	\$14.0m Grant	IDA	Governance Assistance Project The grant will assist Mongolia in <ul style="list-style-type: none"> • Improving the efficiency and effectiveness of Governance processes in the management of public finances; • Promoting transparency and accountability in the performance of public sector functions; and • Fostering the investment climate in Mongolia
23/05/06	\$4.0m Grant	IDA	Rural Education and Development Project The grant is to assist Mongolia to enhance the quality of education in rural primary schools grades 1-5 by improving student access to, and use of, quality learning materials and improving teachers' skills through the promotion of professional networks.
08/06/06	\$8.0m Grant	IDA	Information and Communications Infrastructure Development Project The project will increase the coverage and use of relevant information communication technology services (ICT) among the rural population through an incentive program designed to encourage private operators to provide their services in the rural segment of the ICT market; and to increase private sector participation in the delivery of e-government services, thereby improving public sector utilization of ICT.

b) CONSTITUENCY - WORLD BANK GROUP FINANCED PROJECTS TO 30 JUNE 2006

IDA14 AND GRANTS

With the advent of IDA14, we have seen a change away from borrowing by our Constituency members and more grants being received.

In FY05 Cambodia received a \$20.0m grant in addition to an IDA Loan

In FY06 monies (total \$41.8m) received by our constituency members were in the form of grants:

- Cambodia received a \$14 million grant;
- Kiribati received a \$1.8m grant from GEF; and
- Mongolia received \$26 million in grants for three projects.

WORLD BANK GROUP FINANCED PROJECTS TO 30 JUNE 2006

Year	2001		2002		2003		2004		2005		GRAND TOTALS	
	No of Loans	Total \$ M	No of Loans	Total \$ M	No of Loans	Total \$ M	No of Loans	Total \$ M	No of Loans	Total \$ M	No of Loans	Total \$ M
IBRD												
Papua New Guinea	4	141	1	40							5	181
Total	4	141	1	40							5	181
IDA												
Cambodia	3	63	3	47	4	65.75			2	18	12	193.75
Mongolia	3	69	2	24			1	18	2	18.3	8	129.3
Samoa	1	5	1	4.5			1	2.08			3	11.58
Solomon Islands												
Vanuatu	1	4									1	4
Total	8	141	6	75.5	4	65.75	2	20.08	4	36.3	24	338.63
IFC												
Cambodia			1	3			2	16	1	6 ⁵	4	25.0
Korea	1	50	2	70							3	120.0
Mongolia							2	8			2	8.0
Papua New Guinea									1	3.2	1	3.2
Pacific Islands												
Total	1	50	3	73			4	24	2	9.2	10	156.2

Grand Total: IBRD IDA/ITF and IFC = \$ 675.8 million All figures rounded

⁵ Credit Line of \$ 6.0m

ANNEX 4- CONSTITUENCY MEMBERSHIP**a) Constituency Voting Power - Percentage of Total and Number of Votes as of June 30, 2006**

MEMBER	IBRD		IDA		IFC		MIGA	
	%	#	%	#	%	#	%	#
Australia	1.53	24,714	1.24	195,130	1.98	47,579	1.53	3,300
Cambodia	.03	464	.11	17,283	.02	589	.21	445
Kiribati	.04	715	.07	11,777	.01	262	----	---
Korea Rep. Of	.99	16,067	.60	94,639	.67	16,196	.50	1,072
FS Micronesia	.05	729	.12	18,424	.04	994	.15	331
Marshall Islands	.04	719	.03	4,902	.04	913	---	---
Mongolia	.04	716	.16	24,389	.02	394	.16	339
New Zealand	.46	7486	.29	45,489	.16	3,833	---	---
Palau	.02	266	.02	3,839	.01	275	.15	331
Papua New Guinea	.10	1,544	.25	39,121	.06	1,397	.18	377
Samoa	.05	781	.14	21,850	.01	285	.15	331
Solomon Islands	.05	763	.00	518	01	287	---	---
Vanuatu	.05	836	.09	13,821	.01	305	.15	331
Total	3.45	55,800	3.12	491,182	3.04	73,309	3.18	6,857

CONSTITUENCY MEMBERSHIP

MEMBER	IMF	IBRD	IDA	IFC	MIGA	ICSID	G-77*
Australia	X	X	X	X	X	X	
Cambodia	X	X	X	X	X		X
Kiribati	X	X	X	X			
Korea	X	X	X	X	X	X	
Marshall Islands	X	X	X	X			X
Micronesia FS	X	X	X	X	X	X	X
Mongolia	X	X	X	X	X	X	X
New Zealand	X	X	X	X		X	
Palau	X	X	X	X	X		X
Papua New Guinea	X	X	X	X	X	X	X
Samoa	X	X	X	X	X	X	X
Solomon Islands	X	X	X	X	X	X	X
Vanuatu	X	X	X	X	X		X
TOTAL	13	13	13	13	10	8	9

* Membership has risen to 132 countries but G77 title is retained for its historic significance
Australia and Korea are members of the G20 formed in 1999.

b) CONSTITUENCY VOTING RECORD: 1 JULY 2005 – 31 JULY 2006

During this period the Bank's Group Board of Governors voted on the following resolutions

#	RESOLUTION TITLE	DATE
<i>IBRD GOVERNORS' RESOLUTIONS</i>		
568	Direct Remuneration of Executive Directors and their Alternates	24 August 2005
569	Financial Statements, Accountants' Report and Administrative Budget	24 September 2005
570	Allocation of FY05 Net Income	24 September 2005
571	Transfer from Surplus to Fund Trust Fund for Earthquake Recovery and Reconstruction in Pakistan	07 December 2005
572	Transfer from Surplus to Replenish the Low-Income Countries Under Stress Implementation Trust Fund	21 February 2006
573	Transfer from Surplus to the National Multi-Donor Trust Fund for Sudan and the Multi-Donor Trust Fund for Southern Sudan	21 February 2006
574	Forthcoming Annual Meetings of the Boards of Governors – Proposed Dates for the 2007 and 2008 Annual Meetings in Washington, DC	17 July 2006
<i>IDA GOVERNORS' RESOLUTIONS</i>		
210	Financial Statements, Accountants' Report and Administrative Budget	24 September 2005
211	Additions to Resources: Financing the Multilateral Debt Relief Initiative	21 April 2006
<i>IFC GOVERNORS' RESOLUTIONS</i>		
242	Financial Statements, Accountants' Report, Administrative Budget and Designations of Retained Earnings	24 September 2005
<i>MIGA GOVERNORS' RESOLUTIONS</i>		
73	Financial Statements and Accountants' Report	24 September 2005
74	Reclassification of the Czech Republic	20 June 2006