DEVELOPMENT COMMITTEE

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Development Issues

Presentations to the 44th Meeting of the Development Committee

Washington, D.C.—September 21, 1992

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Joint Ministerial Committee of the Boards of Governors
of the World Bank and the International Monetary Fund
on the Transfer of Real Resources to Developing Countries
(Development Committee)
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Established in October 1974, the Development Committee is known formally as the Joint Ministerial Committee of the Boards of Governors of the World Bank and the International Monetary Fund on the Transfer of Real Resources to Developing Countries. The Committee's members, usually Ministers of Finance, are appointed in turn for successive periods of two years by one of the countries or groups of countries represented on the Bank's or the Fund's Board of Executive Directors. The Committee is required to advise and report to the Boards of Governors of the Bank and the Fund on all aspects of the broad questions of the transfer of real resources to developing countries, and to make suggestions for consideration by those concerned regarding the implementation of its conclusions.

The International Bank for Reconstruction and Development (IBRD) and its affiliate, the International Development Association (IDA), together constitute the World Bank. The International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA) are other affiliates of the IBRD.

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FOREWORD

The Development Committee considered a number of important development issues at its 44th meeting, held in Washington, D.C., on September 21, 1992.

One of the two main agenda items was Resource Flows and Transfers to the Developing Countries on which the World Bank and the IMF prepared a paper for the Committee. Ministers recognized that there was a need to follow up this broad issue by focussing on some selected areas in future meetings. The Committee therefore agreed to review, in their May 1993 meeting, the prospects for increasing flows of private resources and improving the access of developing countries to global markets for loan and equity capital. This review will include the role of the international financial institutions in promoting and catalyzing such flows and the extent of any remaining obstacles placed by developing and industrial countries to such resource flows.

The second main item was a report by the World Bank Group on The Legal Framework for the Treatment of Foreign Investment. This paper included a set of Investment Guidelines on the Treatment of Foreign Direct Investment (FDI). Since the creation and maintenance of a suitable legal framework is an important part of attracting foreign investment, the Committee called them to the attention of member countries, as useful parameters in the admission and treatment of FDI in their territories.

Ministers also took note of progress reports on Trade Policy Developments which included the recent status of the Uruguay Round negotiations; and on the Outcome of the U.N. Conference on Environment and Development and the follow-up action planned. The Report by the President of the World Bank dealt, among other things, with the Status of the IDA Deputies' Negotiations on the IDA-10 Replenishment.

In view of the general interest of these subjects, the papers prepared for this meeting are now published in this pamphlet (available in three languages--English, French, and Spanish) for the benefit of a wider audience.

Peter Mountfield
Executive Secretary
September 1992

STATEMENTS BY THE CHAIRMAN OF THE DEVELOPMENT COMMITTEE
Alejandro Foxley, Minister of Finance, Chile

A. WRITTEN STATEMENT

The September meeting of the Committee will be an important one. Following our discussion of "Development Priorities for the Nineties" a year ago, we shall be considering the first comprehensive review for seven years of the totality of resource transfers to developing countries. We shall also have before us a valuable paper on Investment Guidelines and the usual progress reports.

Economic Background As President Preston's Report reminds us, developing countries as a group have performed reasonably well over the last two years, in spite of a sluggish world economy, although certain areas, especially in Africa, have not shared this experience. Since we shall no doubt be debating this in the Interim Committee and the Annual Meetings which follow, I do not think we should take too much time during the Development Committee meeting talking in general terms about the economic climate. Instead I think our Committee should concentrate on the concrete measures we can take to adapt to this climate. That is why the paper on Resource Transfers is so important.

Resource Transfers Members will recall the background to this paper. The G-24 Ministers, at their meeting in Bangkok, showed great concern about the continued pattern of negative net transfers from the World Bank to developing countries, and called for a study of this trend. The Committee with Mr. Preston's encouragement, decided to commission such a study, but to broaden it out to cover all forms of flows to developing countries. This study covers a very broad canvas indeed. Here are my own reactions to the paper, some of which I should like to reflect in our communique.

(a) Domestic savings are crucial. A better title for the whole paper might be "Finance for Development", since the paper reminds us that the vast bulk investment in developing countries is financed from domestic resources (through taxation or savings). Taking developing countries as a whole, the contribution of ODA, of FDI, and of other forms of transfer is important but secondary; it is valuable as much for its side-effects (technical assistance, management skills, access to technology and to markets) as for its cash value.

(b) A country with a strong current account does not need transfers of external resources on the same scale as countries with chronic deficits. It is more than ever necessary to help developing countries help themselves, by giving them wider access to world markets for their exports.

(c) Disaggregation is important. The paper demonstrates the very different patterns of resource transfer in different regional and economic groupings. In the end, each country must be considered individually, but a few regional generalizations are possible. For example, Sub-Saharan Africa differs from the majority of other developing countries because 90% of its external resource flows take the form of ODA, which is now equal to 8% of the region's GDP, and interest payments on past loans were in most recent years a small part of its total current account deficits. This pattern is completely different from that of Latin America, for example. Generalizations about the totality of developing countries can be dangerously misleading if they lead to calls for global action to correct what are really regional or national problems.

(d) ODA is going to be a very scarce resource, and some of it may be diverted in future away from traditional recipients towards new claimants. I was therefore pleased to see that the recent G-7 Munich Summit agreed to "direct official development assistance more towards the poorest countries" and the leaders promised to "continue their best efforts to increase the quantity <u>and quality</u> (my underlining) of ODA". Similarly the developing countries carry a heavy responsibility for seeing that aid is better spent than in the past.

(e) The multilaterals, and especially the World Bank, will play an increasingly important part in coordinating and redirecting the aid effort. It is important for the Bank to maintain a flow into those recipient countries which still need loan capital and are in a position to use it properly. The poorest, of course, will continue to need highly-concessional or grant assistance rather than IBRD lending, thus avoiding further negative transfers in future.

(f) Syndicated commercial bank lending of the kind which led to the debt crisis of 1982 is a thing of the past (apart from a few special cases). None of us wants to see a return to such heavy reliance on floating-rate debt. For a small number of developing countries, bond finance offers an acceptable substitute. Although bonds are debt-creating instruments, if the proceeds are wisely invested (not just used to finance a current account deficit) the debt can be serviced without difficulty. But we should not look to bank or bond finance as a general source of development funding, still less of balance of payments finance. Nor should we call for unwise modifications in necessary prudential regulation, since a strong and healthy international banking system is in everyone's interests; although some easing at the margin, especially in the crucial area of trade finance, may be possible.

(g) Foreign Direct Investment has increased sharply in the last three years, but it is still heavily-concentrated in a handful of countries. There is no doubt of the benefits it can bring to recipient countries. The Committee has debated in the past the best ways of creating a domestic climate favorable to such investment. On the whole these are also the ways which encourage domestic investment. Where the general climate is favorable, many investors will seek out and invest in profitable opportunities

without too much regard to the precise legal safeguards. But there is no doubt that a clearer and more even-handed legal treatment of foreign investors will help to reassure the investor. That is why the separate paper on Investment Guidelines is so important. There is also an important role for cofinancing with the multilateral development banks and for guarantees of the kind provided by MIGA; we might consider whether the present range of instruments is complete. Perhaps we should reconsider the need for limited (policy-based) guarantees from the multilateral institutions in this area.

(h) Portfolio investment brings fewer immediate advantages in terms of management skills, new technology or access to markets. But there is a case for giving it greater encouragement, both because it helps to tap a wider source of funds (institutional investors in particular) and because of the stimulus it brings to domestic capital markets. I believe we should look more closely at the use of country funds, to which the IFC has already given a useful impetus.

This leads us back to the problem of encouraging and mobilizing local savings. That involves a close study of fiscal policy (including the scope for reducing unproductive government expenditure), monetary policy and local financial institutions. This is a field in which the IMF and the World Bank have given much valuable advice in the past.

There is a great deal of detailed material in this paper, which raises important questions to which the Committee may wish to turn again at a future meeting.

Investment Guidelines The adoption of a firm legal framework to govern foreign direct investment is a necessary but not a sufficient condition for encouraging Foreign Direct Investment. But the proposed guidelines seem to me a useful first step in the direction of providing greater predictability for potential investors. At the same time, they safeguard the essential interests of sovereign host governments. They are not as comprehensive as some critics might like; but they represent much more than the lowest common denominator of existing rules. They are the most coherent statement of contemporary "best practice" that we are likely to achieve immediately. At this stage they are put forward as non-binding recommendations, not as rules. But I share the hope that they will progressively harden into something more binding. I believe it is best to regard them as a stage in the evolution of a more comprehensive treatment at some future date. As such I am glad to commend them to the Committee. The authors point out in the covering note that they are a distillation of the treatment to be given by host governments to foreign investors. Many critics believe they need to be matched by conditions which apply to foreign companies themselves. But since the UN has already done a lot of work on the Transnationals Code, and proposes to do more next year, I see little point in duplicating their efforts here.

Trade It is disappointing to record that little has happened on the trade side since our April meeting. And it is frustrating for the developing countries to sit by and await the outcome of the Uruguay Round which at this

stage is dominated by the industrial countries. But I do not think the Development Committee can resolve the deadlock, although we should once again draw attention to the damage which it inflicts on the developing countries, and add our voice to those (like the G-7 Summit Leaders) who call for a rapid and constructive end to the talks.

Debt Since our last meeting, the G-7 Summit has called for an extension of the enhanced Toronto Terms, on a case-by-case basis, to certain heavily-indebted Lower Middle Income countries. We should of course welcome this development in our own communique.

IDA As the President's Report reminds us, there is still no agreement on the size of the Tenth Replenishment of IDA. There is to be one more meeting of the IDA Deputies immediately before our own and I hope we shall be able to record more progress in our communique, although I understand that final decisions will not be taken until November.

UNCED The progress report ends by summarizing the action to be taken in the Bank and in the Fund in response to the outcome of the Rio Conference. We should note and welcome this.

B. ORAL REMARKS

We meet today at a time of great change and some turbulence in the world economy. The end of the bipolar world and the movement toward market-oriented economic policies offer the potential for greatly enhanced international trade and finance. At the same time, sluggish growth in much of the world, poorly coordinated macroeconomic policies and stagnation of trade talks threaten to undo much of the progress achieved in the last few years. Both of these tendencies have important implications for developing countries.

As we move into the decade of the nineties, there is a danger that we shall repeat some of the mistakes of the eighties. Let us look back again to early 1982. Ten years ago, the Western world was congratulating itself on its success in recycling the oil surplus of the seventies, much of it on-lent by Western banks to developing countries. At the same time, the authorities here in the U.S. were pleased to have gotten their inflationary pressures under control by a steep increase in interest rates. It was the combination of these two events, each of them in isolation a correct response to an external crisis, which provoked the debt crisis later in 1982, and had wholly unexpected consequences for the health of the world banking system, as well as for the developing countries.

Is there, I wonder, a lesson for us in these events? Consider the global economic situation we now face. In the United States, we see an economy still trying to recover from recession, and we witness a reduction in interest rates to record low levels in an attempt to accelerate the process of recovery. In Western Europe, by contrast, we see a group of closely-linked economies which would similarly like to resume faster growth, but which feel compelled--by the threat of renewed inflation--to constantly realign their interest rates and exchange rates. In many countries in both North America and Europe we also see fiscal deficits that are larger than what price stability and growth would call for. The resulting pressures on exchange rates, and on the recovery prospects of some of the European countries, produce a conflict which has not yet been resolved, as current events dramatically confirm. The tendency for exchange rate appreciation in some countries is also leading to renewed calls for protectionism, and is one of the factors which have led to the current standoff in the Uruguay Round negotiations.

This policy standoff has had unintended and unwanted effects on the economic prospects of developing countries. On the trade front, for instance, the absence of further liberalization in developed country markets means that developing countries are losing a unique opportunity to expand their exports. Without the rewards of export growth, countries are finding it hard to take full advantage of the opportunity to liberalize their own economies--indeed, some of them too are threatening to revert to protectionist policies. These policies in turn mean that the industrialized

countries risk losing markets, and the whole global economy moves into a downward spiral instead of starting the virtuous circle of expansion.

Similarly, the monetary policies adopted by many of the industrial countries have had the wholly unintended consequence of precipitating a flood of short term speculative capital into the middle-income economies of Latin America, putting pressure on exchange rates and rendering monetary policy quite difficult to manage. This situation has also the effect of slowing down the process of world growth and feeding back into the economies of the industrial countries themselves.

I am trying to make a very simple point. Sound macroeconomic policies by industrialized countries and a greater degree of policy coordination are in everyone's interest. In this regard there is no need for the developing countries to appeal for social justice of make a call for charity. It is in the interests of the industrial countries themselves that they should consider the indirect as well as the direct consequences of their actions. The world economy today is so interdependent that measures taken by one government in what it perceives as its own best interests can have wholly-unexpected consequences for its own citizens as well as for the rest of the world.

As we move into the middle nineties, there is another element in the equation. For the first time, we have to consider the formerly socialist economies of Eastern Europe and the old Soviet Union as full members of the world economic community. While of course we all welcome this, unreservedly, their arrival on the scene poses new problems. Consider a few aspects of this. The traditional developing countries are deprived of one of the sources on which they have depended for many years. At the same time, the geopolitical considerations which have motivated so much Western aid are less compelling than they were. This threatens a reduction in the total volume of development assistance. Worse than that, there is an obvious risk that funds will be diverted into support for the newly-emergent economies in transition, and away from the traditional aid recipients. On the other hand, the reduction in world tension means that the traditional aid donors can afford to spend more on aid, if the political will to do so is still there. At this stage, it is not clear where the equilibrium will settle. This Committee, which is concerned with the transfer of real resources, must hope that the donor countries will continue to see it in their own interests to maintain, and even to increase, their aid flows.

But not only the wealthier countries bear the responsibility for global economic health. We in the developing countries must face up to our own share of that responsibility. Today we are going to talk about the transfer of resources to developing countries.

The paper before us makes one very important point which is often forgotten. I mentioned it in the written statement which I circulated to you before the meeting, and I want to emphasize it again today. The vast majority of resources for investment come from the domestic resources of the developing countries themselves. It is our responsibility to tap these

resources in the most efficient way possible. That means that we must learn to mobilize our own domestic savings, as well as to make our markets more attractive to returning flight capital and to overseas investors. It means that we must look at our institutional arrangements to make sure that our banks and savings institutions offer a safe home for savings and a return on investments which encourages them to grow. It means that we must help them to reinvest these savings in the most dynamic parts of our economies.

On the whole we are not very good, as Finance Ministers, at identifying these opportunities. Our job is to help markets to discover the most profitable opportunities for themselves. Bus as Finance Ministers we have two responsibilities which we cannot escape. One is to regulate those markets in ways which avoid monopoly. The other is to pursue sensible fiscal policies which ensure sustainable growth without inflation. We must also pursue sensible fiscal policies which ensure sustainable growth without inflation. Until we get our fiscal policies firmly under control and prove able to generate significant public savings, no transfer of resources will be sufficient to meet our development needs.

Of course the changes in the world economy have affected the developing countries in widely different ways. If we look at the figures for developing countries as a group, it seems that we have done surprisingly well in the last two years, while the rest of the world was in recession. Speaking as a Chilean Minister, I suppose that--concerning the external economic environment--we have little to complain about. Our problems at the moment involve trying to contain the potential inflationary consequences of a large inflow of external capital and foreign investment. Many of my Latin American colleagues have similar preoccupations. Few of us would have predicted this ten years ago at the beginning of the debt crisis. But when I talk to African Ministers in this room today, I know very well that problems are very different, although most of them have done fairly well in the last two years, while starting from a very much lower base. The truth is that the developing countries are not a homogeneous group. While it often suits us to talk as though we were, we all face different problems and to some extent we are bound to seek different solutions.

But while we should not underemphasize the differences among us, we should not also overlook our growing similarities. The emerging consensus--and the growing doses of pragmatism--in the development strategy followed by many developing countries is reflected in the increasingly similar policies we are adopting. Reliance on markets for the allocation of resources, a priority on expanding trade and a greater emphasis on targeted social programs and human capital formation are three examples of policies that are today being adopted by growing numbers of countries. That means, among other things, that we face many of the same problems. It would be very inefficient for each one of us to try to reinvent the wheel, and propose wholly new solutions to well known and common problems. In today's world, countries can learn from one another--we can learn from our successes but also from our mistakes. It is in this context that committees such as this one become particularly useful.

PRESIDENT'S REPORT TO THE DEVELOPMENT COMMITTEE

by Lewis T. Preston, President of the World Bank

I. INTRODUCTION

1. At its April 1992 meeting, the Development Committee addressed the major issues on the post-Cold War international agenda. This meeting focusses on capital flows to developing countries -- a key requirement if a range of urgent global issues are to be dealt with successfully. Growth cannot be sustained, poverty cannot be reduced, and the environment cannot be protected without adequate resources. Nor can the new nations of the former Soviet Union successfully effect the transition to market economies without recourse to substantial volumes of external finance. While the bulk of the required resources must come from developing countries' own domestic resource mobilization efforts, external capital must play an important supplementary role. Given the basic mandate of the Committee, it is both appropriate and timely that it take a comprehensive look at the current flow of financial resources to developing countries in order to highlight the main issues requiring attention from the international development community.

2. The staffs of the World Bank and International Monetary Fund have prepared an issues paper for ministerial consideration. There is no need to repeat its central concerns and conclusions here. It is, however, important to be clear about the issues that are of most relevance and concern to the Bank, and about the actions that need to be taken -- by the Bank and others -- to ensure an adequate flow of resources to developing countries over the current decade.

3. This report begins with a discussion of concessional flows. This is the area in which governments can do the most directly and which is crucial for the vast number of poor countries with few or no alternative sources of external finance. It is an area in which the Bank -- through the International Development Association (IDA) -- historically has played a leading role. The discussion includes two progress reports -- one, an update on the current status of the negotiations for the Tenth Replenishment of IDA and the other (for which there is also a free-standing progress report for Members' consideration) an assessment of the implications of the recent United Nations Conference on Environment and Development (UNCED) for future concessional financing of environmental protection initiatives. Regarding the former, the report's main conclusion is that IDA requires a substantial replenishment if it is to continue to discharge effectively the expanding range of its responsibilities toward the low-income countries crucially dependent upon its resources.

4. The report also briefly discusses recent developments in nonconcessional resource flows and their implications for the World Bank. Its main conclusion is that the Bank will need to continue to play an important lending role in the present decade, even as the composition of its borrowers and the nature of their financing requirements undergo some significant changes.

5. Finally, the report brings members up to date on two regional issues with major financial implications. One is the continuing economic transformation in the countries of the former Soviet Union and the current status of the Bank's activities, including its lending program, for the region. The second is the worsening drought in the countries of Southern and Eastern Africa, which requires the mobilization of substantial funds from abroad to assist the affected countries to protect their peoples from its potentially devastating effects. The Bank, in concert with others, is making a major effort in this regard.

II. CONCESSIONAL FLOWS

6. A major focus of our discussion must be the need for increased concessional resource flows. Financial constraints in many donor countries make it difficult for them to contemplate increases in their aid budgets, despite the substantial reductions in military expenditures consequent on the end of the Cold War. In many countries, perennially strong political pressures to devote additional resources to domestic economic and social problems are becoming more intense. Moreover, publics and parliaments in most countries are now demanding more evidence that aid "works" and that it deserves to be given a high priority on national agendas in donor countries. We all have a growing responsibility to report on the progress which has been made in the developing countries, the improvements in health and education, the jobs created, the growth in output and efficiency, and the modernizing of economies and nations. Much remains to be done to eliminate poverty and expand the opportunities for the peoples in the developing countries, especially low-income countries, but aid--while not without its shortcomings-- has repeatedly demonstrated its effectiveness.

7. The provision of substantial volumes of concessional assistance remains a high priority in the post-Cold War era. The need for aid is not declining; it is increasing as the consequence of an increase in the number of countries reliant upon it, the unfinished tasks of development, and the emergence of new global challenges. Declining creditworthiness and per capita incomes have made countries formerly mainly reliant on nonconcessional flows dependent on concessional assistance. The number of low-income countries undertaking comprehensive adjustment programs designed to restore and sustain economic growth has risen, and such countries require strong support on concessional terms if their reforms are to be sustained. In addition, the financing requirements arising from the renewed commitment to poverty reduction and strengthened protection of the environment are substantial.

8. Most of the financing required to meet priority development objectives must come from domestic sources. External finance can play only a supplementary role, and developing

countries must therefore strengthen their resource mobilization efforts. At the same time, we must seek to enhance the effectiveness in both the provision and use of concessional resources. Strengthened aid coordination is one aspect of the effort to improve the quality of development assistance. Other initiatives to do so--such as increasing the proportion of grants in the assistance provided and greater "untying" of aid--should also be vigorously pursued.

9. But even with a maximum effort to increase domestic savings, and the most effective use of external capital, requirements for concessional assistance will grow. Unless the supply of ODA is increased, our commitment to the importance of growth, poverty reduction, and environmental protection will be largely rhetorical. The constraints on bilateral donors are undeniably formidable, but increased commitments should be readily manageable. Aid is a minor part of donors' overall budgetary expenditures -- on average, it is less than 2 percent of central government budgets. Whatever the views -- and they are diverse -- on the merits of the 0.7 percent ODA/GNP target, the fact is that only five of the twenty countries that are members of the OECD's Development Assistance Committee (DAC) have attained it after over 25 years of promises and exhortations to do so. The overall ratio is still only 0.34 percent. Movement toward attainment of the 0.7 percent target on the part of those countries that have not yet attained it would be a major contribution toward ensuring the adequacy of finance for the development efforts of low-income countries. Military expenditures by major industrial country donors still vastly exceed the volume of concessional assistance they provide for economic development, and agricultural subsidies are another largely unnecessary expense. There can be no doubt that aid could be increased significantly if there were sufficient political will, and if the seriousness of emerging global challenges -- including those of migration and refugees -- were matched by an equally serious commitment of aid resources.

10. Recent years have seen a decline in some countries in the proportion of their total aid budgets devoted to multilateral assistance. I believe this does not reflect a judgment of bilateral donors about the efficacy of multilateral assistance and is regrettable. Bilateral and multilateral programs should be seen as complementary, not competitive. Bilateral donors frequently have expertise in specific sectors, have cultivated sustained and harmonious links with individual recipients over many years, and have often been in the forefront of new development emphases. The provision of foreign aid is an important aspect of foreign policy.

11. By the same token, multilateral development agencies offer advantages which are widely acknowledged and which led to their creation and growth. In general, they are able to sustain a comprehensive, well-informed view of overall economic and sectoral conditions in a wide array of countries. More than most bilateral donors, they are able to give greater weight to developmental criteria in allocating resources between and within countries and are better

placed to conduct the policy dialogue with recipients and to coordinate among donors and recipients. This enables them to help create a policy environment in recipient countries which serves to enhance the overall effectiveness of aid.

12. In confronting the development challenges of the 1990s, it will be more important than ever that bilateral and multilateral donors work closely together and strengthen aid coordination with a view toward enhancing aid's overall contribution to development.

The Implications for IDA-10 and an Update on the Status of the Negotiations

13. IDA is a case in point. In recent years IDA has been requested--by donors and recipients alike--to take on numerous additional responsibilities. These include support for the structural adjustment and policy reforms that will enhance growth, poverty reduction, and--most recently--environmental protection. In addition, the number of claimants on IDA resources is increasing. Since the Ninth Replenishment went into effect in FY91, nine additional countries have joined the list of IDA recipients with every likelihood that more will become eligible.

14. These increased demands on IDA have not, however, been accompanied by an increase in donor contributions. Recent growth in IDA net disbursements has been entirely attributable to IDA reflows and the transfer of substantial annual IBRD net income to IDA, since new donor commitments to IDA have been stagnant in the past decade. The increased demands coupled with fixed resources have confronted IDA with difficult decisions about how to allocate scarce resources by country and type of activity.

15. At the April meeting of the Committee, Ministers requested a further progress report from the Bank's President on the status of the current replenishment negotiations. Since the last Committee meeting, support has been received for a large increase in IDA from several important sources. At their Munich summit, G-7 governments called for a "substantial" IDA-10 replenishment.

16. IDA-10 Deputies met in Dublin on July 1-2 (and they will meet again in Washington on September 17-18) to discuss the closely interrelated issues of the size of the replenishment and "burden-sharing." Despite the strain on budgets in almost every donor country, reasonable progress was made at these meetings, although significant issues remain unresolved. (A brief report on the September meeting will be made in my oral statement to members at our meeting.)

17. Two illustrative scenarios for the size of IDA-10 have been discussed: (i) SDR13 billion, which would maintain the real value of IDA-9, and (ii) SDR16.25 billion, which would accommodate the needs of new and reactivating countries and include an "earth increment" to

help borrowers meet the additional costs of undertaking environmentally sustainable development. While many donors favor an IDA-10 of at least SDR13 billion or more, which would at least equal the volume of IDA-9 in real terms, several major donors remain uncommitted. Moreover, support for an earth increment is limited to a few donors which have expressed support for a modest increment provided there were adequate burden-sharing. Further consideration of the increment will now await resolution of the base volume of IDA-10.

18. The IDA Deputies will meet again in mid-November. Despite the remaining obstacles, the seriousness of their deliberations on IDA-10 has been encouraging and I am optimistic that outstanding issues, while difficult, can be resolved. It is vital to reach an agreement by the end of this calendar year if there is not to be a hiatus in IDA's commitment capacity next July. A replenishment at least equal to the volume of IDA-9 in real terms is urgently required. There should be a sizeable real increase above the level of IDA-9 for the reasons indicated above.

UNCED and its Concessional Financing Implications

19. IDA Deputies have generally agreed that IDA-10 should maintain the basic development objectives agreed upon in IDA-9, with emphasis on deepening and integrating IDA's work in priority areas. One such area of increasing IDA activity is assistance to recipients in helping them meet their national environmental objectives, and IDA financing requirements for this purpose were extensively discussed at the historic Earth Summit in June. Other environmental funding initiatives were also discussed at the summit, and I wish to give members a brief update on them. (See the accompanying report to the Committee on the principal outcomes of the Earth Summit and their implications for the World Bank and IMF.)

20. UNCED expressed its support for a number of initiatives previously endorsed by Ministers in the Development Committee meeting last April. These include:

* The conference agreed that the required financing in support of both national environmental action plans and global environmental objectives should be provided through existing institutions rather than new funding mechanisms.

* It asked that special consideration be given to the need for a substantial Tenth Replenishment of IDA to enable it to help the recipients of its resources meet their national environmental objectives, and to the desirability of an earth increment to IDA-10.

* The conference also expressed its support for the work of the UNDP-UNEP-World Bank Global Environment Facility (GEF) and agreed that, adequately restructured, it is the most appropriate mechanism for meeting the incremental costs of relevant activities for achieving progress on several environmental problems of a global character.

* Support was also given for existing aid consortia arrangements, such as World Bank-led consultative groups and UNDP-led roundtables, as mechanisms through which environmental and other development objectives can be integrated in a coherent fashion and consideration given to their financing requirements.

21. These are important and far-reaching conclusions. The great task in the follow-up to UNCED is now to work toward putting the requisite funding in place and to move forward with increasingly effective integration of development activities and efforts to protect the environment. The Bank is fully committed to do so. The incremental funding that will be required to arrest environmental degradation at both national and global levels will be substantial indeed, and much of this will clearly have to be supplied on concessional terms. In the light of the UNCED recommendation, IDA Deputies should again take up the question of an earth increment once the base level of IDA-10 is set (to assure it is truly additional to IDA-10). The poorest countries already face severe environmental difficulties which will be costly to manage. To make sustainable development a reality, they are going to need substantial concessional assistance.

22. At the global level, it is important to proceed with the replenishment of the GEF so that developing countries can meet their global environmental commitments beyond the pilot phase. There was an impressive response in Rio to my urging to replenish the GEF during 1993 and, in their statement to the plenary, the heads of state of several industrial countries supported a two- to threefold increase in resources for it.

III. NONCONCESSIONAL FLOWS

23. Concessional flows are of critical concern to the poorest developing countries. But their scarcity means that special efforts must be made to increase flows of other types of resources to all countries. Resource transfers of a nonconcessional nature present an increasingly complex and challenging set of issues. I would like briefly to direct the Committee's attention to these and their implications for IBRD.

24. Domestic resource mobilization efforts are also crucial in the countries that are primarily reliant on nonconcessional flows. Their dependence on external financing is much lower than that of borrowers on concessional terms. With appropriate domestic policies in place, they should be able to ensure access to the supplementary external nonconcessional resources, from both private and official sources, that they require for their development efforts. However, a number of other factors -- including poor economic growth in industrial countries, debt servicing difficulties and trade barriers -- have acted as constraints on resumed creditworthiness and growth. Further efforts are required to conclude debt reduction agreements between those severely-indebted middle- and lower-middle-income countries undertaking adjustment programs and their commercial-bank creditors, assisted as appropriate by the World Bank and IMF. Improved economic growth in industrial countries would greatly improve developing countries' growth, export performance, and debt-servicing capacity. On the trade front, a successful conclusion to the Uruguay Round of multilateral trade negotiations is of the utmost importance because it would bring substantial benefits to many middle-income countries with considerable export capacity and potential.

25. Recent years have seen significant changes in the sources of nonconcessional resource flows to developing countries. One is the substantial shift in finance from debt to equity. In 1985, foreign direct investment represented less than 8 percent of total financing and only a little more than 20 percent of private flows to developing countries. In 1990, however, foreign direct investment accounted for over 22 percent of total flows and over 50 percent of private flows, obviously largely a result of the decline in commercial bank lending. A report on the Legal Framework for the Treatment of Foreign Investment has been prepared for the Committee in response to its request in its April 1991 meeting. Attached to this report is a set of guidelines submitted for recommendation to member countries. These guidelines were prepared by the General Counsel of the Bank, the IFC and MIGA, after broad consultation with international organizations, business councils, and international law associations--and have benefitted from the comments of the Executive Directors of the Bank and MIGA on earlier drafts.

26. A second significant development is the reinvigorated use of older financial instruments (e.g., portfolio investment) and the proliferation of newer ones (e.g., debt-equity swaps, bonds with special features, structured project finance, and other innovative financing such as commodity-linked finance).

27. While these are welcome developments, they are far from touching all countries. As the issues paper on resource transfers prepared for this meeting of the Committee indicates, flows of foreign direct investment remain heavily concentrated in relatively few countries. From 1981-91 half of all flows of foreign direct investment went to the five largest recipients, and 90

percent was accounted for by 20 countries. Not surprisingly, similar concentration ratios hold for some of the newer kinds of resource transfers, i.e., there is a strong tendency for them to flow to more creditworthy countries in the middle-income group.

28. These and related developments have led to a situation in which the universe of recipients of nonconcessional flows has become increasingly differentiated. Economic circumstances, and thus the capacity to access capital markets, vary greatly across countries. As noted, some countries have dramatically improved their access to private capital and now have little reliance on flows from official nonconcessional sources (such as IBRD), e.g., a number of countries in East Asia. Others, including several of the so-called Brady countries, have managed to restructure their debt substantially while making significant adjustments to their economies to enable them to ensure access to commercial markets. Numerous other middle-income and lower-middle-income countries, however, have limited creditworthiness and will find their access to private external finance crucially dependent on continued progress with policy reforms. They currently have a demand and capacity for increased borrowing which must be met in large part from official nonconcessional sources since most of them have little access to flows on concessional terms. In addition, a number of low-income "blend" countries (i.e., recipients of both IBRD and IDA resources) can be expected to increase their reliance on official nonconcessional finance as they continue to grow, successfully reduce poverty, and implement policy reforms that make them increasingly able to service debt on harder terms, but their access to commercial markets remains limited. The external capital requirements of the countries of the former Soviet Union are another factor making for an increasingly complex array of recipients.

Some Implications for the World Bank Group

29. These developments have a number of implications for the future work of the World Bank Group. The Bank's relative share of financing should appropriately decline in those countries where poverty has been reduced and access to private capital has been improved. Indeed, by the end of the decade some of them will rely exclusively on the international capital market. The situation is different in the many countries where creditworthiness has slipped and access to private capital remains relatively slight. For these countries, IBRD lending remains an important source of finance. Moreover, since it is clear that continued policy reform is crucial to renewed creditworthiness, the Bank must play a key role in helping its borrowers undertake necessary reforms through a constructive policy dialogue supported by economic and sector work and technical assistance. Increasingly, countries seek policy advice from the Bank. The increased consensus about the nature of appropriate policy reforms in borrowing countries has served to enhance the Bank's policy role. In addition, the Bank's role as a catalyzer of flows from other sources, and especially from private sources, will necessarily take on added

importance in the future. The growing role of the International Finance Corporation also marks an increasingly significant contribution.

30. Although lending from IBRD, measured in constant dollars, has stagnated since 1982, it became a much larger share of the total, as private capital flows declined. IBRD lending became increasingly differentiated and conditioned by individual country circumstances and policies. Country conditions characteristic of the past decade--including previous overborrowing by many countries on world capital markets, the deterioration in their external environment associated with world recession and the debt crisis and the consequent reduction of public and private investment, and the initial inadequacy of reform efforts in some countries--sharply limited the Bank's ability to finance productive operations in many countries. Such factors are less likely to be at work in the present decade, the opportunities for increased IBRD lending can therefore be expected to mount, and a growing IBRD lending program can make an essential contribution toward meeting the external financing requirements of countries implementing reform programs.

IV. DEVELOPMENTS IN THE COUNTRIES OF THE FORMER SOVIET UNION AND THE WORLD BANK'S ROLE

31. The President's Report to the Committee last April outlined the steps the Bank is taking in response to the dramatic developments in the new nations emerging from the break-up of the former Soviet Union. Since then events have unfolded at a rapid pace. To date, eight countries which were formerly part of the Soviet Union have become members of the Bank. (Some have also become members of IDA and IFC.) The remainder whose membership applications are still pending are also expected to become members in the near future.

32. The countries of the former Soviet Union all face daunting development challenges, although the nature and severity of these differ from country to country. Economic output in the former Soviet Union has declined by about 25 percent over the past year. Inter-state trade has dropped by perhaps more than 50 percent over the last two years. A severe economic crisis characterized by large budget deficits, rising inflation rates, and a major erosion of living standards is at hand. Deep-seated structural distortions in their economies make the way forward likely to be long and difficult.

33. The Bank is actively engaged in assisting the new nations make the transition to market economies. In this regard, it is coordinating its activities closely with those of the IMF,

and this has greatly facilitated the assistance process. Close coordination is also taking place with others involved in helping the new nations' reform efforts. The Bank's recruitment process for staffing positions devoted to work on the region has been accelerated and is now almost complete -- a substantial achievement in so short a time. Regional missions are being opened in four locations to facilitate implementation of the Bank's assistance strategy. The strategy over the medium term entails a number of priority elements, including: to halt, and then reverse, the precipitous economic decline; assist in the structural transformation of the economies of the region into market-oriented systems; support sector-specific reforms for building productive capacity, focusing initially on areas where a quick supply response is essential (especially energy and agriculture); strengthen social safety nets for protecting the disadvantaged during the reform process and assist in labor force restructuring; and develop the human resource skills and institutional capacity necessary for supporting a market-based economy. It will also be important to assist with the design and implementation of a broad array of financial sector reforms.

34. The effort entails a substantial commitment to economic and sector work as well as technical assistance in each of the new nations. A comprehensive country economic memorandum on Russia was issued in July, and similar introductory economic reports on each country will be circulated to the Bank's Board, either before or simultaneously with the submission to the Board of the first Bank lending operation in the respective country. These will help to provide a solid factual and analytical basis for the policy dialogue with each new borrower.

35. There are clearly a great many risks on the road ahead. These include the danger of a weakening of the political commitment to reform, which could lead to policy slippages; inadequate implementation capacity; and shortfalls in the availability of external financing. The challenges are unusual and daunting, but the Bank is determined to work closely with the new nations to confront them successfully.

36. Assistance to the new Bank members will involve a substantial lending program. A lending program of about $2.5 billion is envisioned this fiscal year. The Bank's first loan to Russia in the amount of $600 million for a rehabilitation program and in support of current reform efforts was approved by the Board of Executive Directors on August 6. Other loans for Russia, the Baltic states and Central Asian countries are in an advanced stage of preparation. As indicated in the President's Report to the Committee last April, the Bank's aggregate lending program in the new nations could grow to a level of $4-5 billion per annum by FY95. This is contingent, of course, on the momentum of reform being maintained.

37. An additional requirement is the need for appropriate external assistance coordination mechanisms for those new borrowers engaged in major structural reforms. A number of

alternative institutional arrangements are being explored together with the IMF, some modelled along the lines of the consultative groups which the Bank chairs for many developing member countries. Membership in each group would be determined case-by-case.

38. While the Bank undertakes this broad array of activities in the new countries, it continues to focus on its global responsibilities. The Bank's contribution--a substantial one--toward meeting the financial requirements of its new members will be made without reducing the resources available to its traditional developing country borrowers. Helping countries of the former Soviet Union to achieve economic transformation is, however, as great a challenge as any the Bank has faced in its history. The Bank will bring to bear on it the vast body of experience and knowledge gained over many years in its work throughout the developing world. Setbacks and disappointments can be expected along the way, but ultimately great benefits are anticipated from the integration of the new nations into the international economic system. Moreover, these will accrue to all countries--not only to the reforming nations themselves.

V. POVERTY AND DROUGHT IN SOUTHERN AND EASTERN AFRICA

39. One clear example of the Bank's continuing commitment to its borrowers throughout the developing world is its recent response to the current drought in Southern and Eastern Africa. The latest drought only serves to exacerbate conditions in many countries of Sub-Saharan Africa, where the number of people living in poverty was already on the increase. (For the region as a whole, the population in poverty is estimated as likely to increase from 180 million in 1985 to 265 million in the year 2000.) The drought demonstrates once again how prone the region is to natural catastrophes that swell the ranks of the poor. Conditions in the affected countries continue to deteriorate as the drought's devastating effects take hold, putting at least 18 million people at risk from starvation and disease in Southern Africa. The affected countries of Southern Africa are estimated to have food import needs of 11.5 million metric tons this year compared with less than 2 million in a normal year. In Eastern Africa, severe drought conditions also exist in a number of countries and are exacerbated in some by intense civil strife.

40. The Bank is actively involved in assisting the drought-stricken countries of the region and is working closely with the United Nations, which has rightly received universal commendation for its coordinating role. The Bank participated in the emergency meeting of concerned parties on Southern Africa held in Geneva in early June, at which $526 million in additional resources was pledged for drought relief. Efforts continue to increase this figure to the goal of $900 million and it is important that they succeed. There is, however, no room for

complacency. Governments will urgently need to dismantle regulations and barriers to the free flow of goods; enhance internal distribution systems; improve collaboration with nongovernmental organizations; and set aside political differences to ensure food reaches those in need. Donors will need to expedite specific commitments and expeditiously turn commitments into aid deliveries. International agencies need to enhance coordination in support of specific sectors, notably the transport sector, and ensure that assistance reaches intended recipients.

41. For its part, the Bank is increasing its own assistance to the affected countries; late in FY92, for example, the Bank committed an additional $310 million in quick-disbursing assistance on IDA terms to Malawi, Mozambique, Zambia and Zimbabwe. We anticipate continuing such support in FY93 for these and other countries affected by the drought both by building on planned adjustment and investment operations and, on the request of borrowers, by reallocating available funds from approved operations. The Bank is cooperating closely with the United Nations and regional institutions like the Southern Africa Development Coordinating Committee (SADCC) and the Inter-Governmental Authority on Drought and Development (IGADD). The Bank will continue to monitor the situation closely and report on additional needs through the consultative group process, in direct consultations with bilateral aid agencies, and in on-going interactions with the authorities in the affected countries.

VI. SUMMARY AND CONCLUSIONS

42. The multiplicity of current development challenges is unprecedented. New global concerns entail many additional responsibilities even while the traditional tasks of ensuring economic growth and reducing poverty remain high on the development agenda. The central message of this report is that an increased volume of external resources will be one crucial ingredient for ensuring that the complex challenges of our era are successfully met. Such resources cannot substitute for the resolute efforts of countries in the developing world. They can tip the balance, however, toward success. Working closely with our borrowers, I am confident that we can successfully assist them to surmount the obstacles that currently impede many countries in the attainment of their development objectives.

WORLD ECONOMIC SITUATION AND ECONOMIC TRENDS IN DEVELOPING COUNTRIES

Statement by Michel Camdessus,
Managing Director of the International Monetary Fund

The external economic environment for most developing countries is expected to improve in the second half of 1992 and in 1993, owing to an anticipated rebound in industrial country activity, stronger growth of world trade, continued low international interest rates, and a modest recovery in non-oil commodity prices. Oil prices are expected to remain at their current relatively low levels, which should help contain import costs for the majority of developing countries.

The cautiously optimistic assessment of the outlook for world output and trade presupposes that those developing countries that are implementing stabilization and structural reform policies will continue to do so, and that there will be a pickup in growth in industrial countries. The outlook for the industrial countries is, however, subject to considerable uncertainty. Thus far, the recovery in the industrial countries has been weak and uneven and it may take some time before the current economic slack is absorbed and growth in the industrial countries is sufficiently strong to underpin a recovery of primary commodity prices. The projections also assume the avoidance of increased protection through managed trade arrangements and other barriers to trade, and that efforts to achieve a more open multilateral trading system will continue.

World economic activity showed signs of revival in the first half of 1992, following stagnation in 1991 and growth of 2 1/4 percent in 1990. World output is expected to expand by 1 percent in 1992 and 3 percent in 1993, close to the average of the past two decades (Table 1). The global slowdown in 1991 reflected weaker growth in the industrial countries as a group--including recession in the United States, the United Kingdom, and Canada--stagnation in the Middle East, and a sharp contraction of output in Eastern Europe and the former U.S.S.R. Growth in the industrial countries is projected to increase to 1 3/4 percent in 1992 and 3 percent in 1993, with the recovery expected to gather strength during the next twelve months.

After an expansion of nearly 6 1/2 percent in 1989, growth in the volume of world trade fell from about 4 percent in 1990 to 2 1/4 percent in 1991, reflecting the cyclical slowdown in import demand by industrial countries and the collapse of trade between the countries of Eastern Europe and the former Soviet Union. The growth of world trade is likely to increase to 4 1/2 percent in 1992 and 6 1/2 percent in 1993, owing in part to the expected gradual recovery of economic activity in the industrial countries.

Table 1. Industrial, Developing, and Former Centrally Planned Economies: Major Economic Indicators, 1989-93
(Annual changes in percent, except where noted)

	1989	1990	1991	1992	1993
World					
Real GDP growth	3.3	2.3	0.1	1.1	3.1
Trade Volume	6.8	3.9	2.3	4.5	6.7
Trade Prices					
Fuel	21.5	28.3	-17.0	0.0	-0.6
Nonfuel primary commodities[1]	-0.6	-7.8	-4.5	1.4	2.8
Manufactures	-0.2	9.0	-0.5	4.6	3.5
Six-month dollar LIBOR (percent)	9.3	8.4	6.1	3.9	4.2
Industrial countries					
Real GDP growth	3.3	2.4	0.6	1.7	2.9
Inflation	4.4	4.9	4.4	3.3	3.2
Import volume growth	7.3	4.5	2.4	4.1	5.1
Developing countries					
Real GDP growth	3.7	3.6	3.2	6.2	6.2
Inflation	70.2	80.2	42.5	42.4	27.7
Inflation (median)	9.6	10.0	8.6	7.8	6.1
Current account (in billions of U.S. dollars)	-16.0	-14.2	-78.2	-51.8	-52.9
Current account (in percent of exports)	-1.8	-1.4	-7.3	-4.5	-4.1
Export volume growth	7.1	4.9	7.6	8.1	9.3
Import volume growth	8.0	5.4	9.3	8.5	9.6
Terms of trade	1.7	2.1	-3.6	-1.8	0.2
Export unit value	5.2	7.8	-2.3	0.6	2.9
Import unit value	3.4	5.6	1.4	2.4	2.7
Debt (in billions of U.S. dollars)	1206	1281	1362	1427	1473
Debt (in percent of exports)	132.8	125.6	126.5	122.9	113.4
Debt service (in percent of exports)	16.1	14.2	14.5	14.5	14.3
By region					
Africa					
Real GDP growth	3.2	1.0	1.5	1.9	3.3
Inflation	18.7	16.2	27.1	28.6	18.6
Current account (in percent of exports)	-7.4	-1.9	-3.6	-9.0	-7.0
Export volume growth	6.2	3.3	2.2	2.9	5.0
Import volume growth	1.6	0.6	-3.0	5.8	2.6
Terms of trade	-0.9	3.9	-6.2	-6.3	-1.3
Debt (in percent of exports)	236.7	221.3	230.5	237.0	227.2
Asia					
Real GDP growth	5.3	5.5	5.7	6.9	6.6
Inflation	13.1	8.7	9.0	8.4	8.1
Current account (in percent of exports)	0.3	-0.3	-0.7	-1.6	-1.8
Export volume growth	6.8	7.9	12.3	10.2	11.7
Import volume growth	9.9	8.0	12.5	10.9	11.9
Terms of trade	0.6	-1.5	-0.0	-0.7	-0.2
Debt (in percent of exports)	70.4	69.1	68.4	66.1	62.2
Middle East					
Real GDP growth	3.8	5.4	0.3	9.9	8.7
Inflation	17.8	16.6	22.1	16.4	16.5
Current account (in percent of exports)	-1.4	-1.7	-24.6	-2.9	-1.5
Export volume growth	9.2	-1.7	0.0	5.2	5.3
Import volume growth	5.5	2.0	0.5	0.1	5.9
Terms of trade	7.9	13.1	-11.3	-1.3	2.0
Debt (in percent of exports)	135.4	122.7	134.2	133.0	121.6
Western Hemisphere					
Real GDP growth	1.0	-0.1	2.9	2.8	3.9
Inflation	434.3	649.7	163.2	178.9	87.6
Current account (in percent of exports)	-5.5	-4.3	-12.1	-15.0	-14.8
Export volume growth	6.4	4.6	4.0	6.1	6.4
Import volume growth	8.4	3.1	16.9	10.6	8.1
Terms of trade	0.5	-0.5	-4.7	-3.4	0.6
Debt (in percent of exports)	262.6	251.8	269.2	267.1	247.9

Table 1. *(Concluded)*

	1989	1990	1991	1992	1993
By Analytic Criteria					
Countries with recent debt-servicing difficulties					
Real GDP growth	2.0	-0.6	-0.3	4.5	6.2
Inflation	218.6	295.2	109.9	116.0	62.3
Current account (in percent of exports)	-8.8	-7.2	-10.7	-13.4	-12.7
Export volume growth	6.1	-1.2	-1.0	5.4	8.9
Terms of trade	0.8	1.7	-5.6	-3.6	-0.2
Countries without recent debt-servicing difficulties					
Real GDP growth	4.7	5.5	5.2	6.6	6.3
Inflation	13.2	10.5	12.3	12.9	13.2
Current account (in percent of exports)	-1.5	-1.9	-1.9	-3.6	-3.6
Export volume growth	7.3	8.1	11.0	10.6	11.6
Terms of trade	0.6	-0.3	-0.0	-1.2	-0.2
Fuel exporters					
Real GDP growth	3.9	4.7	1.5	8.7	7.9
Inflation	18.1	15.4	18.1	12.1	9.2
Current account (in percent of exports)	-4.6	-0.9	-25.2	-10.9	-8.7
Export volume growth	10.7	1.7	2.7	4.7	5.2
Terms of trade	9.2	14.4	-12.9	-3.3	0.8
Exporters of nonfuel primary products					
Real GDP growth	0.1	1.4	3.3	4.1	4.5
Inflation	290.9	265.9	87.4	37.0	22.4
Current account (in percent of exports)	-15.8	-13.1	-19.0	-21.0	-17.9
Export volume growth	9.2	10.5	3.5	6.1	7.3
Terms of trade	-4.1	-6.2	-4.4	-4.4	0.3
Exporters of manufactures					
Real GDP growth	4.6	3.5	4.5	5.7	5.9
Inflation	97.8	129.8	59.6	79.7	49.3
Current account (in percent of exports)	2.9	1.1	1.4	0.7	-0.3
Export volume growth	5.0	5.8	11.3	10.1	11.3
Terms of trade	0.4	-2.1	0.5	-0.4	-0.1
Former Centrally Planned Economies					
Real GDP growth	2.0	-1.5	-9.7	-16.8	-4.5
Inflation	18.3	21.2	95.4	1192.4	109.6
Current account (in billions of U.S. dollars)	-4.4	-22.4	-9.7	-18.6	-24.6
Current account (in percent of exports)	-2.2	-11.9	-6.7	-14.8	-17.3
Export volume growth	-2.2	-21.1	-22.5	-12.4	12.9
Terms of Trade	1.0	8.1	-2.1	-1.4	-0.4
Debt (in percent of exports)	77.0	89.8	122.3	153.5	151.3
Debt service (in percent of exports)	10.9	18.1	19.8	12.7	12.3
Eastern Europe					
Real GDP growth	-0.2	-7.1	-13.7	-9.7	2.4
Inflation	130.6	142.2	134.9	796.4	42.1
Current account (in billions of U.S. dollars)	2.5	-1.4	-6.4	-2.9	-4.2
Current account (in percent of exports)	3.1	-1.9	-9.7	-4.1	-5.5
Export volume growth	-5.3	-12.1	-20.4	1.0	8.8
Terms of Trade	0.7	-7.1	-5.2	5.2	0.6
Debt (in percent of exports)	126.5	146.4	166.8	162.3	148.9
Debt service (in percent of exports)	17.6	15.2	18.0	15.3	13.6
Former USSR					
Real GDP growth	2.5	-0.4	-9.0	-18.2	...
Inflation	2.3	5.4	88.9	1296.2	...
Current account (in percent of exports)	-5.7	-18.3	-4.2	-27.7	...
Export volume growth	-0.4	-25.3	-24.1	-23.5	...
Terms of Trade	1.2	17.0	-0.4	-5.9	...
Debt (in percent of exports)	45.1	53.2	84.9	142.8	...
Debt service (in percent of exports)	6.6	19.9	21.3	9.4	...

[1] In U.S. dollars. Averages weighted by 1979-81 commodity shares in exports of developing countries or groups of countries.

The aggregate terms of trade of developing countries fell by 3 1/2 percent in 1991, largely because of a 17 percent decline in oil prices and a 4 1/2 percent drop in non-fuel commodity prices. In 1992, the terms of trade of these countries are expected to deteriorate a further 1 3/4 percent on account of an increase in import prices despite a small increase in non-fuel commodity prices and no projected change in world oil prices. The overall movements in fuel and non-fuel commodity prices in 1992 imply varying movements in the terms of trade for different groups of countries. Countries that primarily export non-fuel primary commodities will experience their fourth successive annual decline, with a cumulative loss of 19 percent. The terms of trade of fuel exporting countries are expected to decline 3 1/4 percent in 1992, following a drop of 13 percent in 1991, reversing much of the sharp increase in 1989-90. In contrast, the terms of trade of countries that primarily export manufactures are projected to decline marginally, following a small increase in 1991.

Interest rates in most international capital markets have fallen significantly over the last year. The average six-month dollar LIBOR declined from 8 1/2 percent in 1990 to 6 percent in 1991, and averaged 3 1/4 percent in July 1992. The declines in interest rates reflect a policy response to generally weak economic conditions and a more favorable inflation performance in the industrial countries. Short-term interest rates fell significantly in the first half of 1992 in the United States, Japan, and Canada; in contrast, they continued to firm in Germany, France, and Italy. Long-term rates in the major industrial countries generally declined, albeit by significantly less than short-term rates. Interest rates are expected to change relatively little during the next twelve months.

Economic trends in the developing countries

Output in the developing countries expanded by 3 1/4 percent in 1991 and is expected to rise by 6 1/4 percent in both 1992 and 1993, supported by stronger growth in the industrial countries, a reduction in debt-servicing costs associated with the decline in international interest rates, a rebound of economic activity in the Middle East, and the continued effects of improved policies. Rapid growth is projected to continue in Asia, assuming the current slowdown in Japan does not seriously affect export growth of countries in the region. Somewhat stronger growth is expected in Africa, although the severity of the drought in the southern part of Africa is likely to continue to have a marked adverse effect in that region, and projected growth in Africa remains below that in other regions. Growth in the Western Hemisphere is projected to increase to around 3 1/4 percent during 1992-93, compared with 2 3/4 percent in 1991 and an average of less than 1/2 of 1 percent during 1988-90. This improved performance reflects, in large part, the implementation of sound policies in many countries in the region.

Average inflation in the developing countries was halved to about 40 percent in 1991-92 and is projected to recede further to about 30 percent

in 1993; the more representative median inflation rate is expected to decline from 8 1/2 percent in 1991 to 6 percent in 1993. Inflation has declined dramatically in the Western Hemisphere as a result of adjustment programs and fiscal consolidation in several countries. Inflation in Asia has been roughly unchanged during the last two years; upward pressure on prices in several countries due to capacity constraints and excessive credit expansion has been offset by a decline in inflation in a number of other countries following restrictive monetary policies. Inflation is also expected to decline in some Middle Eastern countries to rates that prevailed before the conflict in the region. In Africa, inflation is projected to remain relatively high in 1992 due in part to increases in administered prices and high public sector deficits in several countries. The drought in southern Africa is also expected to put upward pressure on prices.

After rising by 5 percent in 1990, the volume of exports by the developing countries increased by nearly 8 percent in 1991 as a sharp increase in intra-regional exports by Asian countries more than offset a slowdown in export growth elsewhere. Countries that export mainly manufactures increased export volumes by 11 1/4 percent in 1991, while countries that export mainly primary products increased export volumes by 3 1/2 percent in 1991. Developing countries' exports are expected to rise further by 8 3/4 percent in 1992-93 as the pace of activity strengthens in the industrial countries. In 1992-93, export growth is likely to stabilize at around 10 3/4 percent for exporters of manufactures, 6 3/4 percent for exporters of nonfuel primary products, and 5 percent for fuel exporters.

The aggregate current account deficit of the developing countries increased sharply from $14 billion in 1990 to $78 billion in 1991. Although influenced by cyclical developments in the industrial countries and by a worsening of the terms of trade, this widening was caused primarily by the effects of the crisis in the Middle East. There was also a significant increase in deficits in the Western Hemisphere reflecting in part a real exchange rate appreciation and a sharp increase in capital goods imports. The current account deficit of the developing countries is projected to decline to an average of $52 billion in 1992-93. Although the current account deficit of the Middle Eastern region is expected to decline sharply as a result of the normalization of oil production, the external deficits of many other developing countries are projected to increase, partly in response to strong capital inflows.

The total external debt of the developing countries rose by 6 1/4 percent during 1991 to reach $1,362 billion. The debt-to-export ratio was virtually unchanged in 1991 at 125 percent, and is expected to decline in 1992-93 to an average of 118 percent. This ratio has declined significantly since 1986 because of improved economic performance, reduced borrowing, and debt reduction operations. The most pronounced reductions have taken place in Western Hemisphere, while the improvement in Africa has been considerably smaller due in part to relatively low growth of export earnings.

Since 1986, the reductions in the debt-service ratio for the developing countries have also been pronounced, falling from 23 percent in 1986 to 14 1/2 percent in 1991. The decline has been particularly sharp for the group of fifteen heavily indebted countries, several of which have benefitted from the Brady initiative; their debt-service ratio fell from 45 percent in 1986 to 31 percent in 1991. During 1992-93, debt-service ratios are likely to remain broadly unchanged as increases in the ratios for the Western Hemisphere and African countries are offset by declines in Asia and the Middle East. In the African countries, the increase is likely to be due to the accumulation of arrears and continuing low growth of export earnings due to declining terms of trade and lagging reform efforts in several countries.

During the first half of 1992, debt restructuring agreements were successfully completed for several developing countries. In June, Argentina and representatives of creditor banks announced agreement on final terms for reducing medium and long-term foreign bank debt and past-due interest. The Philippines also signed an agreement with commercial banks involving a combination of new financing, a restructuring of existing debt, and debt buybacks. Nigeria completed a debt-restructuring agreement during the first half of the year, which reduced medium-term foreign debt by $3.4 billion. An agreement in principle has been reached on a debt and debt-service reduction package covering Brazil's $44 billion of medium- and long-term obligations to foreign commercial banks. Mexico announced in June 1992 the cancellation of $7 billion of its foreign debt, which it had acquired mainly through buybacks and debt conversions. In addition, twelve developing countries concluded debt restructuring agreements with official creditors, consolidating more than $17 billion of debt-service obligations.

The successful experience of a number of middle income countries in handling their debt problems in recent years has confirmed that the key ingredient for graduation from reliance on exceptional financing is the sustained implementation of sound policies. Backed by substantial debt and debt-service reduction agreements, which served as a catalyst, these countries have regained access to private financing and have increased prospects for future growth.

For many other countries debt service problems remain severe. This group includes some lower middle-income countries where macro-economic imbalances have been particularly large, the record of policy implementation uneven, and levels of indebtedness to official creditors particularly high. In addition, progress of low-income countries towards viability has in general been slow, even for those that have established a relatively strong policy track record.

Economic Trends in Eastern Europe and the former U.S.S.R.

In Eastern Europe, economic conditions improved during the first six months of 1992 in the Czech and Slovak Federal Republic, Hungary, and Poland. There was a substantial increase in their exports to convertible

currency markets and a number of industries were beginning to compete successfully with imports. These developments indicate that the supply side of these economies is responding to systemic reforms and to the opening up of these economies to international trade and investment during the last two years. In contrast, output continued to decline in other countries in the region, because of continuing difficulties with the transformation process and, in the case of Yugoslavia, civil war. In 1993, moderate growth is expected in Eastern Europe as a whole for the first time since 1988, as stronger export markets and improved domestic conditions should stimulate production in a number of sectors.

Following a small decline in inflation in 1991, higher fiscal deficits in some countries as well as further price liberalizations and the effects of the war in Yugoslavia pushed up the inflation rate in 1992. However, inflation is expected to fall in 1993, owing to the diminishing impact of price liberalization, tighter monetary policies, and wage controls.

The aggregate current account deficit of Eastern Europe is projected to narrow from $6 1/2 billion in 1991 to $3 billion in 1992. In 1991, the deficit was lower-than-expected because imports were compressed due to a lack of foreign financing and depressed domestic demand. The reduction of the deficit expected in 1992, would reflect relatively strong exports from Poland, Czechoslovakia, and Hungary, and by weak imports due to continued financing constraints in other countries.

Net financial flows are expected to rise from $2 1/4 billion in 1991 to $3 1/2 billion in 1992, and to increase further to $6 1/4 billion in 1993. Direct foreign investment, although still modest, surged in 1991 and the first half of 1992 in Hungary and Czechoslovakia, but remained subdued in most other countries. Official creditors still account for the bulk of the capital inflows, although improvements in underlying performance and creditworthiness, as well as stronger reserve positions, have allowed some countries to gain access to private sources of capital. The total external debt in Eastern Europe remained broadly unchanged in 1991 as the impact of the debt restructuring agreement between Poland and the Paris Club offset increased borrowing from official sources by other countries in the region.

Economic conditions in the former U.S.S.R. continued to deteriorate and output in the region is projected to contract by about 18 1/4 percent in 1992, following a similar decline of 9 percent in 1991. Real output in Russia is estimated to have fallen by 14 percent in the first half of 1992 compared with a year earlier. Output in Ukraine is likely to decline by over 20 percent in the first half of 1992. In the Baltic states, output declined sharply in 1991, partly because of shortages of petroleum products from Russia, and a further decline of nearly 30 percent is expected in 1992. 1/

1/ Disaggregated projections for the former Soviet Union for 1993 are not available.

The liberalization of most consumer and producer prices early in 1992 caused an additional jump in the overall price level following steep price rises in 1991. In Russia, retail prices are estimated to have increased more than eight-fold in the first half of 1992. Recent policy measures aimed at fiscal consolidation should help to dampen price increases in the second half of the year, although inflation is still likely to remain very high.

Exports from Russia to countries outside the territory of the former Union are reported to have fallen some 30 percent in the first five months of 1992. The actual decline could be less, however, since a growing fraction of exports may not be reflected in official statistics. Imports are estimated to have fallen by 14 percent. Preliminary projections point to a combined current account deficit for the 15 countries of the former Soviet Union of $15 3/4 billion in 1992 and $20 1/2 billion in 1993; these figures are conditional on sizable external financial support.

Net financial flows are projected to rise to $21 billion in 1992 following flows of $9 1/4 billion in 1991. Contributing to the increase are transfers by Germany, related to the repatriation of former Soviet military personnel, and substantial borrowing by Russia from official creditors under the assistance package committed by the international community. The increase also assumes a moderate buildup of foreign currency holdings after the depletion that occurred in 1990. The total external debt increased in 1991 to some $66 billion, but the debt-export ratio jumped from 53 percent to 85 percent as trade collapsed; further increases in the debt ratio are expected for 1992.

STATEMENT BY THE CHAIRMAN OF THE GROUP OF TWENTY-FOUR
Alhaji Ahmadu Abubakar
Minister of Finance and Economic Development, Nigeria

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1. On behalf of Ministers of the Group of Twenty-Four, I would like to submit to the members of this Committee the main points in the Communique issued by the G-24 Ministers at the end of their deliberations on the issues before your Committee.

2. Ministers of the Group of Twenty-Four considered the issue of resource flows to developing countries, and noted that although aggregate net resource flows to these countries increased moderately in real terms in 1991, they are still far below the levels achieved in the early 1980s. They, therefore, called on the international community to supplement the domestic resources of these countries by adequate provision of financial flows to improve their prospects for sustainable growth and poverty reduction.

3. Ministers expressed concern that in spite of appeals and promises since the past twenty-five years, the overall ODA/GNP ratio is only 0.34 percent. They commended the efforts of those donor countries that have reached and surpassed the agreed target of 0.7 percent and reiterated their call on the others to take urgent steps to achieve the target. They stressed the need for much larger and highly concessional resource flows to the low-income and lower-middle-income sub-Saharan African countries in view of the problems of widespread poverty, low levels of savings and investment, excruciating debt service burden, and the recent severe drought and famine in these countries.

4. Ministers recognized the potentials of foreign direct investment (FDI) in increasing resource flows to developing countries and called for increased effort by the industrial countries and multilateral financial institutions to accelerate the growth of FDI. They also called on governments of developing countries to make their environments conducive to FDI inflow and capital repatriation.

5. Ministers welcomed the report by the World Bank entitled "Legal Framework for the Treatment of Foreign Investment," which provides non-binding and adaptable guidelines for developing countries. They reaffirmed their view that the guidelines should not lead to an additional Bank lending conditionality.

6. On the Uruguay Round, Ministers underscored the need for developing countries to increase earnings from trade and thereby reduce their dependence on the developed countries for financial assistance. They stressed the importance of an open trading system to the flow of resources to developing countries and emphasized the need for a speedy and successful completion of the Uruguay Round in order to improve market access for developing countries.

7. Ministers noted the outcome of the recently concluded United Nations Conference on Environment and Development held in Rio de Janeiro, Brazil,

and emphasized the need for concerted action and shared responsibility to effectively address global environment and development issues. They stressed that a very substantial amount of resources is required to implement the decision of the conference. They underscored the need for industrial countries to assume greater share and the necessity for new and increased financial flows to developing countries on highly concessional terms in order to promote environmentally sustainable growth and poverty reduction in these countries. Ministers stressed that national environmental problems in many developing countries are often a consequence of widespread poor living conditions. They, therefore, called on the multilateral development institutions to increase their concessional financial flows above the current levels in order to deal effectively with poverty which is a major cause of the problem.

8. On IDA-10 Replenishment, Ministers called attention to the positive role IDA has played in stimulating growth, reducing poverty and protecting the environment, as well as the expected large increase in demand for IDA resources in the 1990s and emphasized the need for a substantial increase in its replenishment, which should be significantly higher in real terms than IDA-9. They urged donor countries to respond positively before the end of 1992.

9. Ministers welcomed the recent recommendation of the Executive Boards of the Fund and the Bank to increase the number of seats on the Boards of both institutions to accommodate the growing number of new members. They, however, emphasized the need to continue to preserve the true multilateral character of the Bretton Woods institutions and reaffirmed their call that the geographical representation, voting power and number of seats of the present developing countries in the two institutions should at least be maintained, if not increased.

RESOURCE FLOWS TO DEVELOPING COUNTRIES

(Prepared jointly by staff of the World Bank
and the International Monetary Fund)

SUMMARY AND ISSUES FOR DISCUSSION

(i) Resource flows to developing countries have undergone unprecedented changes over the past decade. In the wake of the debt crisis, a precipitous drop in resource flows in the early part of the decade was only partially reversed in the latter part. The sources of flows showed a strong shift from private to official and, within private, from debt to equity and from bank to non-bank investors. These changes took place in the context of the end of the Cold War, greater integration of global capital markets, and widespread market-oriented structural reforms in developing countries. This is a timely occasion for the Development Committee to review recent trends in resource flows to developing countries and the need to improve their access to external finance.

(ii) Within the overall decline in net flows, there were important differences in the patterns of flows across regions and, within regions, across countries reflecting differences in levels of income, economic performance and creditworthiness. Aggregate net transfers--a measure that must be used with caution for reasons noted in Appendix I--were positive in 1991 for the third consecutive year. However, for countries with substantial commercial bank indebtedness, notably in Latin America, net transfers continued to be negative, though less so towards the end of the decade.

(iii) Official creditors provided extensive financial support to developing countries, including those in debt servicing difficulties, through concessional and nonconcessional loans, grants and debt forgiveness. In rescheduling for low-income countries, the Paris Club has recently implemented a menu of enhanced concessions ("enhanced Toronto terms"), and put in place a procedure for considering possible debt stock reduction after a three-year period. The July 1992 G7 Summit in Munich encouraged the Paris Club "to recognize the special situation of some highly indebted lower-middle-income countries on a case by case basis." However, a number of severely indebted low- and lower-middle-income countries continue to face very uncertain prospects for medium-term viability.

(iv) Official development assistance (ODA) flows have grown steadily (about 3 percent a year) in nominal terms since 1982.[1] However, in real terms, after some increase earlier in the decade, ODA flows have stagnated throughout the decade, and have remained well below the target of 0.7 percent of GNP.

(v) A recent phenomenon is the very rapid growth in portfolio flows--that is, purchases of financial securities such as stocks and bonds--especially to the private sector in selected Latin American and East Asian countries. This is a welcome development given that middle-income developing countries will need to rely primarily on private sources for meeting their external financing needs in the 1990s. On the supply side, increased integration of global capital markets has brought industrial countries' investors more centrally into developing country financing; and macroeconomic stability and improved investment climates have induced the return of resident capital held abroad. On the demand side, increased financial integration and private sector reform have permitted private firms in developing countries to access

[1] *In this paper, references to ODA flows exclude debt relief.*

international bond and equity markets directly.

(vi) However, the outlook is for continued tightness in capital markets, characterized by limited access for developing countries, and increased differentiation by creditworthiness in the terms of borrowing for those countries that do have access. As in the 1980s, in the coming decade developing countries will have to rely primarily on domestic savings, and in some instances the return of flight capital, to finance by far the major part of their investments. Low-income countries may be able to continue to count upon positive net transfers. In the increasing competition for funds, however, a key for developing countries to attract greater flows will be to foster improved confidence in the domestic private sector. That, in turn, requires policy action regarding macroeconomic stabilization and the progressive dismantling of domestic barriers to capital flows. Many donor governments are also paying attention to issues of good governance.

(vii) In this context, Ministers may wish to consider the following issues:

- Developing countries will need to rely on domestic savings to fund by far the major part of their domestic investment.

Are satisfactory policies in place by and large in developing countries to encourage the mobilization and efficient use of domestic savings, including the repatriation of flight capital? What particular policies and institutions have proved particularly effective in achieving these objectives?

- The success of developing countries in reforming their economies and ensuring an appropriate level and composition of external financing will depend in large part on the strength and stability of the global economy. Factors that would tend to lower real interest rates on average (over business cycles) are fiscal consolidation and improved public savings performance in major industrial countries, and structural reforms in these countries, especially those relating to the removal of subsidies and other distorting trade mechanisms.

Do Ministers agree that sustained expansion in the economies of the industrial countries, a non-inflationary environment and low real interest rates, and trade policies that provide open and secure access to markets, are critical to ensuring the success of developing countries' efforts and providing a more conducive context for increasing financial flows?

- Foreign direct investment (FDI) is potentially a large and growing source of non-debt financing, with considerable concomitant benefits (primarily technology transfer). Many developing countries will need to be more effective in attracting substantial flows of FDI, if they are to obtain adequate financing and close the technology gap.

Apart from improving creditworthiness, how should developing countries attract FDI more effectively? What specific additional measures should be implemented to remove domestic barriers to FDI, by easing regulations, strengthening institutions, and liberalizing the financial sector? Can source countries beneficially influence the flows through microeconomic measures, such as taxation agreements, as well as through open trade to

help improve investors' confidence in making longer-term decisions? [2]

- Portfolio equity flows so far have been concentrated in only a few developing countries and have tended to be volatile, as reflected in domestic stock market prices.

Do the benefits of portfolio capital flows warrant a progressive opening of capital markets in developing countries? To what extent can multilateral institutions assist developing countries by catalyzing and encouraging private-source flows?

- Commercial bank syndicated lending to developing countries is unlikely to be an important source of financial flows as in the past decade. Banks are rather shifting to short-term trade and project financing, and bond financing has increased in importance.

What steps can policymakers take to facilitate continued bank lending in these new forms? How do the countries concerned assess their access to the bond market and how can more developing countries obtain access to these forms of financing?

- Despite progressively greater official debt relief, a number of severely indebted lower-middle-and low-income countries that have pursued adjustment programs continue to meet only a fraction of their external debt-servicing obligations.

Are the mechanisms that have been established sufficient to assist these countries in their return to external viability? What further steps may be needed?

- ODA flows have stagnated in real terms in recent years at a time of exceptional demands arising from the growing number of countries adopting structural reforms, non-traditional recipients and environmental concerns. Official finance and better economic performance could act as a catalyst to private flows. Additionally, for poorer countries, concessional official flows have a central role for poverty reduction and supporting structural reform efforts. There is a need to increase and demonstrate the effectiveness of aid spending, including focussing aid on low-income countries with strong policy reforms and poverty reduction strategies. An increase in aid directed at such countries would provide a strong signal of international support for developing countries' own efforts.

Do Ministers agree that, in view of the emerging new and exceptional demands, additional steps are needed in aid decisions by donors and recipients to promote better quality and use of scarce aid flows? Given increased attention by developing countries to policy reforms, do Ministers agree that there is a compelling case for a substantial increase in official aid? Do Ministers agree that there is substantial scope for reallocating aid to low-income countries pursuing effective strategies for growth and poverty reduction?

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[2] *These issues are also addressed in the Development Committee Paper, "Legal Framework for the Treatment of Foreign Investment", which is being prepared for the Fall 1992 meeting.*

- Multilateral institutions, particularly the Bank and the Fund, have played a key role in supporting reform policies, providing policy advice and coordinating aid. The need to enhance aid effectiveness suggests that these efforts should be strengthened. This implies, as endorsed by the July 1992 G7 Summit, that negotiations on a substantial replenishment of IDA funds should be concluded before the end of 1992 and that the IMF should continue to provide concessional financing to support the reform programs for the poorest countries; and that, following the recent one-year extension of the ESAF, there should be a full examination of the options for the subsequent period, including a successor facility.

Do Ministers agree that the urgency of supporting reform efforts, the growing infrastructure and environmental needs, and the coordinating role of the multilateral institutions point to both a speedy replenishment of IDA-10 at an increased real level of resources; and early completion of the full examination of the options for a successor to the ESAF?

I. INTRODUCTION

1. The unprecedented changes in recent years in the world economic system have led to radical shifts in the size and pattern of external flows to developing countries, and greater sensitivity to creditworthiness on the part of investors. Developing countries receive a comparatively small part of total global flows and for them the major determinant of resource flows is their own economic performance. Over the past decade, the pattern of those flows has changed dramatically, with a growing share of official flows, and a strong shift from debt to equity flows and from bank to non-bank sources. In part this reflects the aftermath of the debt crisis, in part the market-oriented structural reforms that have attracted investment to the domestic private sector.

2. In this context, it is timely to examine resource flows to developing countries, a topic which is at the center of the mandate of the Development Committee. This paper examines recent trends in external finance for developing countries by country categories (Section II) and by source of financing (Section III), and in Section IV discusses, for developing and industrial countries, the policies required to increase global savings and, in a resource-constrained environment, to promote resource flows to--and the effectiveness of resource use in--developing countries. A final section (Section V) discusses the role of official multilateral institutions.

II. RECENT TRENDS IN EXTERNAL FINANCE FOR DEVELOPING COUNTRIES BY COUNTRY CATEGORIES

3. The last decade has witnessed fundamental changes in the pattern of resource flows to developing countries. Aggregate net resource flows[1] (in real terms) dropped precipitously from a peak in 1981, as a consequence of the abrupt reduction in bank lending following the onset of the debt crisis. Although official loans and grants as well as FDI showed an increase in real terms, it was not until 1987 that the decline in aggregate net flows was reversed. Since then the recovery in net flows has been led by increasing official flows in support of adjustment programs and a reemergence of private capital flows, particularly in the form of FDI (Chart 1 and Annex Table A1-- as noted in footnote 1, short-term debt and portfolio equity flows are excluded). Aggregate net transfers[2] followed a similar trend (Annex Table

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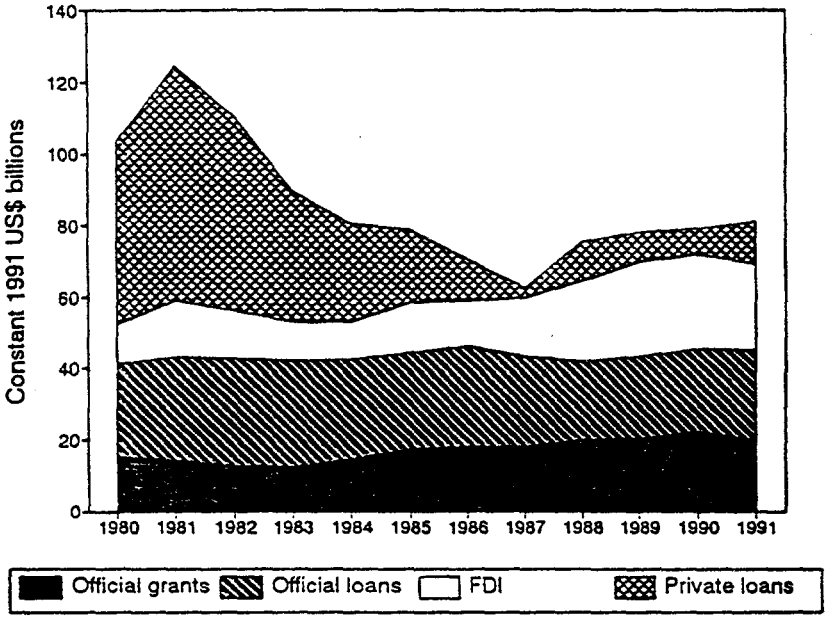
[1] *Aggregate net resource flows are defined on a cash basis, as in the World Debt Tables, as net flows on long-term debt plus net foreign direct investment plus official grants; these flows exclude debt relief except for its impact on an actual cash flow basis. Net resource flows are thus a measure of the external resources available to developing countries to finance deficits on current account transactions (excluding official transfers, which are treated here as a component of flows), the accumulation of reserves, and private capital outflows. The data do not include private grants, for which geographic breakdowns are not available, and portfolio equity flows, for which adequate data are not available. Technical assistance and estimated ODA debt forgiveness were excluded from official grants. Real flows are nominal flows deflated by the import unit value index produced by the IMF.*

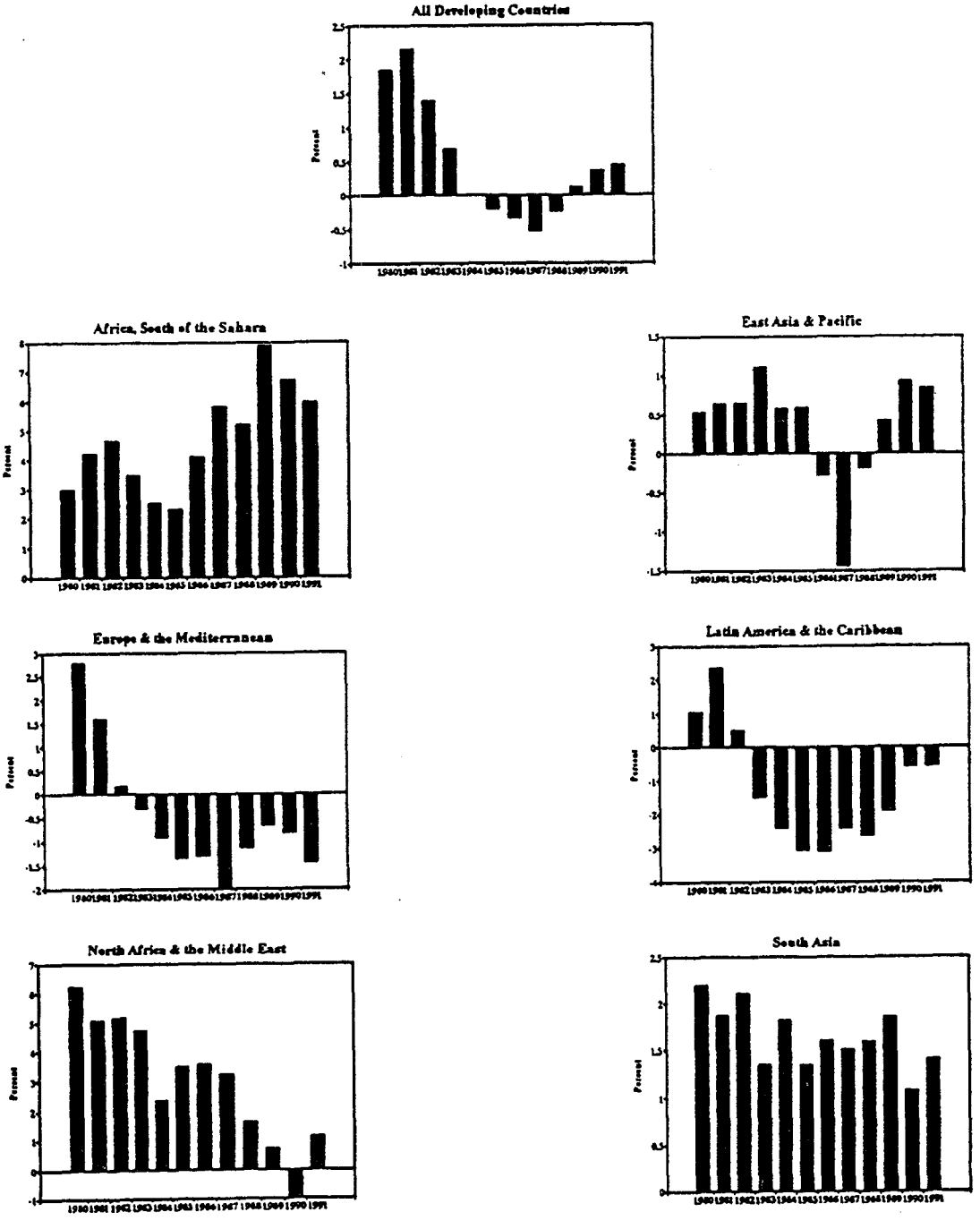
[2] *Net transfers are defined as net resource flows less interest payments on long-term loans and remitted profits on foreign direct investment. Net transfers are a measure of the cash transferred to developing countries as a result of all international transactions and thus represent the external resources available to finance developing country trade deficits--precisely, the current account deficit less interest paid and less remitted profits on foreign direct investment--reserve accumulation, and private capital outflows.*

Chart 1. Aggregate Real Net Resource Flows to Developing Countries, 1980-91
By Source



A3). After being negative in the middle years of the 1980s, net transfers turned positive for the last three years (Chart 2 and Annex Table A4). The concepts of aggregate net flows and net transfers are further explained in Appendix I.

Chart 2. Aggregate Net Transfers as a Percentage of GNP, 1980-91, by Geographical Region



4. Most geographical regions have experienced rising current account deficits and have increased reserves since 1987, while the opposite held true in the mid-1980s. These trends are the counterpart to the fall and subsequent rise in net flows to developing countries. While the direction of changes has been similar for most regions, the trends in financing sources and the direction of causality between current account changes and external resource flows have differed widely.

5. **Sub-Saharan Africa** has experienced a decade of generally rising development assistance (both flows and debt relief) and declining private flows. The share of ODA has greatly increased over the decade, while access to private markets has all but disappeared (apart from short-term trade finance). Currently, net flows represent a high proportion of GNP, and their concessional nature (i.e. a high grant element) together with debt restructuring have resulted in continuing strongly positive net transfers.

6. **Latin America** has experienced sharp swings in current account deficits and international reserves throughout the 1980s. The loss of capital market access in 1981 and the accompanying large decline in net inflows was reflected in a fall in current account deficits through enforced import compression. Since 1987, net resource flows have risen, highlighting the degree to which macroeconomic performance and improvements in the investment climate can attract both private and official flows. As the bulk of Latin America's external debt is on commercial terms, high interest payments have resulted in net transfers being consistently negative, though less so in recent years reflecting in part the fall in world interest rates.

7. Countries in **East Asia and the Pacific** generally experienced small current account deficits throughout much of the 1980s. With improved export performance and availability of external resources, thanks to high credit standing, they were able to build up reserves at a rapid rate. In the late 1980s, however, net flows declined because of a decline in demand. Several countries in the region retired significant amounts of debt, some of it before maturity, notably in 1987. The pattern of external financing sources also shifted over the decade, with both FDI and official nonconcessional loans greatly increasing in importance. Concessional flows have remained very small.

8. **South Asia** experienced generally rising though moderate current account deficits over the decade. The pattern of net resource flows has been much more stable than in other regions. ODA has consistently accounted for more than half of net flows, while commercial bank and bond flows have been significant, though slightly declining in real terms. FDI has remained small throughout the decade. Net transfers have been consistently positive and roughly constant in real terms.

9. **Europe and Central Asia** consists of three distinct groups: the countries of the former Soviet Union (FSU), the formerly centrally-planned economies of Eastern Europe, and the developing market-economies in other parts of Europe. The three groups of countries experienced different patterns of current account balance and access to external finance over the past decade.

10. The FSU experienced current account surpluses up to 1988 and deficits thereafter. Reserve transactions were minimal, except for 1990 when two thirds of the US$21 billion current account deficit was financed from reserves. In spite of current account surpluses, net medium- and long-term resource

flows were positive in years preceding 1988 (abstracting from the USSR's substantial lending to the developing world) as large increases in long-term borrowing from official sources offset sharp drops in net borrowing from commercial banks.[3]

11. The Eastern European countries as a group moved to a current account surplus early in the 1980s, only to revert to a deficit in the 1990s. Aggregate net resource flows declined sharply and turned negative in the late 1980s, but have since turned modestly positive. Net transfers, however, have remained consistently and substantially negative since the onset of the debt crisis in 1982. The picture for net transfers to Eastern Europe has thus been similar to, and has dominated, that for Europe and the Mediterranean as a whole (see Chart 2), i.e. excluding the FSU.

12. The other developing European countries (a heterogenous group consisting of Turkey, Malta, Portugal, and Cyprus) experienced a declining current account deficit throughout the 1980s, which eventually turned to a surplus. A recent sharp drop in exports, however, led to a current account deficit in 1991. A substantial build-up of international reserves in the late 1980s was more than offset by a huge reduction associated with the Gulf War. Net resource flows have been positive and net transfers have fluctuated between positive and negative levels.

13. The capital importing countries of the **Middle East and North Africa** moved from a position of current account deficit to one of surplus at the end of the last decade, reflecting in part reduced access to external flows. The great bulk of flows have been accounted for by ODA. Net transfers have been much smaller at the end of the decade than at its beginning.

14. **Severely Indebted Countries**. Among severely indebted countries, net resource flows to low-income countries (SILICs) have risen steadily over the last decade thanks to growth in official concessional flows and improved economic performance. Net transfers to SILICs have been consistently positive and have experienced uninterrupted growth since the mid-1980s. The pattern of net flows and transfers to low-income countries as a whole has been similar to that for the SILICs, but of about twice the size.

15. Net resource flows to severely indebted middle-income countries (SIMICs) generally declined up until the end of the decade, when the trend was interrupted, thanks in part to substantial bond issuance (particularly by Latin American borrowers). Since the start of the debt crisis in 1982, net transfers to SIMICs have remained strongly negative.

16. A more detailed description of these trends in external finance is given in Appendix III.

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[3] *Macroeconomic data for the FSU are taken from the IMF's World Economic Outlook (WEO), May 1992. The annex tables on resource flows do not include the FSU figures because of lack of comparable data on a long-run historical basis. The country coverage of the annex tables is shown by region in Appendix II.*

III. RECENT TRENDS IN EXTERNAL FINANCE FOR DEVELOPING COUNTRIES BY SOURCE

A. Private-Source Financing

17. **Commercial Banks.** Commercial bank lending was the main form of private-source external finance for developing countries in the 1970s and early 1980s. With the onset of the debt crisis in the early 1980s, commercial bank flows declined sharply before stabilizing at a low but positive level in the second half of the decade. However, interest payments to commercial banks greatly exceeded these net new inflows of capital and as a result, their net transfers to developing countries were negative to the amount of more than US$20 billion per year between 1984 and 1991.

18. A complete picture of commercial bank financing needs also to examine debt restructuring, which has had a major impact on both debt stocks and debt servicing over the past decade. Between 1987 and 1991, the dollar value of long-term commercial bank claims on developing countries has declined from just over US$400 billion to less than US$300 billion (in terms of the face value of loans outstanding). Aside from repayments and exchange rate adjustments, several factors have contributed to this decline. First, debt and debt service reduction operations in Chile, Costa Rica, Mexico, Nigeria, the Philippines, Venezuela, Uruguay and several other countries have reduced the face value of commercial bank claims by about US$20 billion. Second, these same debt reduction operations have resulted in the conversion of about US$60 billion in bank claims (i.e. loans) into bonds; to the extent that these bonds are sold to non-bank investors, bank debt, though not overall debt of developing countries, is reduced. Third, debtor countries have used debt conversion mechanisms, including debt-equity swaps, to extinguish over US$25 billion of external debt owed to commercial banks. The secondary market for developing country debt, which has grown in trading volume and efficiency in recent years, has facilitated the implementation of the debt conversion programs.

19. Commercial bank syndicated lending to sovereign borrowers is not likely to dominate financial flows to developing countries in the foreseeable future. There have been prudential constraints on bank capital imposed by capital adequacy guidelines, while the attractiveness to banks of syndicated loans to developing countries has been reduced by two factors: a desire to avoid the overlending of the 1970s and the early 1980s, and provisioning requirements for loans to borrowing countries with past debt servicing difficulties. For these reasons, banks are shifting to short-term trade and project financing and fee-based transactions, where they have a direct link to a customer, a better debt servicing record and greater security. These are likely to be the main forms of new commercial bank lending to developing countries.

20. **Bond Markets.** In contrast to syndicated credits, bond financing will become a more important form of external financing for developing countries. Through the 1980's, a handful of developing countries have maintained access to the bond markets, of which the most important are Turkey, Korea and Hungary. More recently, countries emerging from debt servicing difficulties have found a receptive market for their bond issues. Between January 1990 and April 1992, developing countries issued about

US$23 billion of new bonds in international markets, constituting an estimated 10 percent of net resource flows over this period (Table 1). Most of these bonds were issued through Euromarkets or through private placements in the United States. In addition, debt reduction operations in six countries have resulted in the creation of bonds with a face value of almost US$60 billion (as noted above). After significant debt and debt service reduction and successful and sustained economic adjustment, Chile and Mexico have regained access to a variety of external financing sources, notably bond markets, foreign direct investment and portfolio flows. Brazil and Argentina have also gained access to new credit flows, in anticipation of debt reduction agreements[4], and more recently Uruguay has had modest access to external financing.

Table 1. International Bond Issues by Developing Country Borrowers
January 1990-April 1992
(US$ millions)

	1990	1991	1992 (to April)	Total
Argentina	21	795	265	1,081
Brazil	-	1,476	1,165	2,641
China	-	274	150	424
Hungary	947	1,316	883	3,146
India	523	274	-	797
Indonesia	825	335	74	1,234
Korea	1,515	2,447	986	4,948
Malaysia	200	190	-	390
Mexico	2,105	2,306	546	4,957
Turkey	660	640	365	1,665
Venezuela	207	262	600	1,069
Others	298	551	619	1,468
Total	**7,301**	**10,866**	**5,653**	**23,820**

Sources: OECD, IMF, and World Bank staff estimates

21. Bond issues have some potential advantages over syndicated credits for both borrowers and lenders. They allow developing countries to tap a wider array of investors than is possible through

[4] *Subsequently, commercial bank creditors reached agreement on terms with Argentina in June 1992, and an agreement in principle was reached with Brazil in July 1992.*

syndicated credits. In addition to commercial banks, these investors include the debtor country's own domestic residents with assets abroad and institutional investors, such as insurance companies, mutual funds, and pension funds. For creditors, bonds have traditionally been perceived as senior to syndicated credits in the event of debt servicing difficulties, although for that same reason their issuance may reduce the debtor country's financial flexibility.

22. The terms of new bond issues have differed widely across borrowing countries. Issuers in countries perceived as less creditworthy have paid wide spreads in recent years, as high as 8 percentage points over industrial country bond yields, and have received relatively short maturities. But the experience of a few countries has shown that spreads can fall very rapidly and maturities can lengthen markedly as markets become comfortable with borrowers and as country creditworthiness indicators improve. Recent bond issues by Mexican borrowers were floated at a spread around 200 basis points; comparable bonds had been issued at more than 400 basis points spreads in early 1990. Some of the new borrowers have used various techniques to reduce their perceived credit risk, especially in the early stages of renewed market access, including collateral (often in the form of an income stream of foreign currency earnings), early redemption options, and equity conversion rights.

23. **Foreign Direct Investments**. FDI in developing countries has almost tripled from its low point of US$8 billion in 1984 (Table A1). FDI flows remain relatively concentrated in a few developing countries: from 1981 through 1991, half of all FDI flows to developing countries went to the five largest recipients. Relative to recipient country GDP, however, the concentration is less marked. The major recipient countries have generally taken measures conducive to foreign investment, including maintenance of macroeconomic stability, exchange and trade policy liberalization, private sector development, and rationalization of the investment regime. The growing flow of FDI to countries in Latin America emerging from debt difficulties illustrates that sustained adjustment policies contribute to access to FDI.

24. FDI, within an appropriate regulatory framework, is important to developing countries not only as a source of external financing but for important nonfinancial benefits. FDI can contribute to human capital creation, provide developing countries with access to scarce technology, and can bring with it marketing links and management know-how. In a number of developing countries, FDI has been a driving force in the expansion and diversification of manufactured exports (for example, Thailand, Malaysia, and China), leading to improved international competitiveness of host economies. And FDI flows can induce other private source financing.

25. **Equity Portfolio Flows**. Over the past few years, non-FDI equity flows have provided a few developing countries with a growing source of external financing. The size of these flows in 1990 and 1991 has been large, running to several billion US dollars, though not easily quantifiable. The benefits of equity portfolio flows are twofold: first, they widen the investor base that developing countries can access; second, they tend to enhance the efficiency of domestic financial markets by importing international prices for financial assets. These flows have taken three major forms: depository receipts that trade on industrial country markets, direct purchases of equity shares on local developing country markets, and country funds.

26. American depository receipts (ADRs) are negotiable equity-backed instruments that are traded on U.S. securities markets. Global depository receipts (GDRs) are similar but can be traded simultaneously on several industrial-country equity markets. Since 1990, developing countries have raised an estimated US$8 billion through ADR and GDR issues. The US$2 billion ADR issue by Telephonos de Mexico (Telmex) in 1991 became a landmark deal, prompting a series of subsequent ADR programs by other Mexican firms and by companies from other developing countries. The dramatic surge of new ADR issues by developing country firms was supported by strong performances in many emerging stock markets.

27. Several countries currently allow at least limited direct purchases of local equity shares by foreign investors. Some permit free entry of foreign investors and unrestricted repatriation of income and capital; these countries include Argentina, Brazil, Colombia, Jordan, Malaysia, Pakistan, Peru, Portugal, and Turkey. Less reliable data are available on this form of investment, but indications are that external resource inflows via this mechanism have been significant recently.

28. Country funds have channeled an estimated US$5 billion to developing countries since the mid-1980s, about US$1 billion in 1991 alone. Most of the funds are closed-ended: once an initial public offering is made, the amount available for investment is fixed. Initial investors may liquidate their holdings through secondary market trades of the fund, rather than withdrawal of the funds from the recipient country which may be difficult because of market illiquidity or regulatory prohibition. Country funds appear to work best as a first step in opening local stock markets to foreign investors and are generally appealing to individual and some institutional investors who lack professional knowledge in emerging markets. Since its pioneering work on the Korea Fund in 1984, IFC has played a significant role in promoting the issuance of country funds.

29. A potential problem with portfolio inflows is their volatility. Nevertheless, their potential size suggests that portfolio equity flows are likely to continue to grow in importance as a source of development finance. For example, U.S. institutional investors held financial assets of over US$6 trillion at end-1991 and the annual increment in these assets is about US$400 billion. Even a small shift of this portfolio towards increasing investments in emerging stock markets could raise significantly the level of capital flows to developing countries.

30. **Nongovernmental Organizations.** A special category of private source flows is Nongovernmental Organizations (NGOs), which consists of significant technical assistance and includes support from official sources. NGOs continued to be an important source of private grants for developing countries over the last decade. Nominal flows from NGOs have steadily increased from US$2 billion in 1981 to an estimated almost US$5 billion in 1991. More than 4,000 NGOs in industrial countries mobilize financial and human resources for development projects, which they operate independently or in partnership with international agencies or counterparts in developing countries. Many industrial country governments have developed various cofinancing schemes for NGO projects.

B. Official-Source Financing

31. Official creditors have provided strong and growing support to developing countries over the past decade in a variety of forms, including the provision of new nonconcessional money, debt relief, and concessional financing. Financing by official bilateral creditors has included direct bilateral lending largely on concessional terms, grants, official support for export credits and other loans, and cofinancing with multilateral institutions. Multilateral creditors have also extended concessional credits and nonconcessional loans to developing countries.

32. **Official Debt Relief.** Official bilateral creditors have assisted countries with debt servicing difficulties by rescheduling pre-cutoff date debt service, mainly through the Paris Club, and through ODA debt forgiveness initiatives implemented on a bilateral basis. Creditors have provided, where needed, comprehensive cash-flow relief and have recently moved towards concessional rescheduling for the low-income countries.[5] In response to the deep-rooted balance of payments difficulties of most of the poorest rescheduling countries, Paris Club creditors adopted in 1988 a menu with concessional options ("Toronto terms"). Through 1991, 20 debtor countries obtained 28 reschedulings on Toronto terms, consolidating debt obligations of some US$6 billion with an average grant element of over 20 percent on nonconcessional debt (representing a decrease in total scheduled debt service of about 2.5 percent, on a present value basis). A further step was taken in December 1991, when the Paris Club agreed to implement a new menu incorporating enhanced concessions in reschedulings for low-income countries. The new menu provides for a 50 percent reduction in the net present value of non-ODA consolidated debt-service payments.[6] So far, seven countries have benefitted from these new rescheduling terms, and the consolidated amount reached almost US$2 billion. The new approach also provides for possible consideration of debt stock reduction after a period of three to four years. For the lower middle-income countries, Paris Club creditors lengthened repayment maturities in 1990 to 15 years. In early 1991, they also conducted far-reaching debt rescheduling agreements with Egypt and Poland in response to the exceptional situation of these countries. The communique of the July 1992 G7 Heads of State Summit, held in Munich, encouraged the Paris Club "to recognized the special situation of some highly indebted lower-middle-income countries on a case-by case basis." Bilateral official creditors not participating in the Paris Club have also provided significant relief to severely indebted countries.

33. **Export Credits.** Official support for export credits could be viewed as official-source financing because, although these credits are largely provided by banks and suppliers, they would not be forthcoming in the absence of an official guarantee. Net export credit flows declined steadily from more than US$9 billion in 1981 and were negative during 1986-88. Since then, however, there has been a

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[5] *As noted in footnote 1 on page 1, the impact of such debt relief on the net flow figures is shown only on an actual cash flow basis in this report.*

[6] *This compares with the "Trinidad terms" as originally proposed by then British Chancellor of the Exchequer Major at the September 1990 Commonwealth conference in Trinidad and Tobago, which entailed the cancellation of two thirds of the stock of pre-cutoff date debt and the restructuring of the remaining one-third.*

recovery and export credits are likely to emerge as an important source of development financing in the coming years. Over the period 1988-91, net export credit flows averaged about US$3 billion. Three factors have been important in reversing the trend of the late eighties. First, many export credit agencies (ECAs) have been moving to a system of risk-based fees, so that export credit cover is now available, albeit at higher cost, to countries perceived as risky. Second, ECAs are likely to provide a larger share of guarantees for loans to private sector borrowers but without debtor country government guarantee. This reflects the growing role of the private sector in many developing countries. Third, official bilateral creditors have pursued a strategy of subordination of old debt to new by maintaining cutoff dates in Paris Club debt reschedulings. This has allowed creditors to extend new credits to countries that have yet to emerge from the rescheduling process but that pursue strong adjustment programs.

34. **Multilateral Institutions.** Net flows from multilateral institutions, both concessional and non-concessional, have been the largest source of lending to the developing countries and their share in total net flows has increased over the past decade. Net flows have averaged about US$13 billion per year, as gross disbursements and amortization payments have increased in line. The medium-term outlook is for increasing net flows in support of structural reforms and the development process in a growing number of countries, including the new borrowing member countries in Eastern Europe and Central Asia. Funding for these emerging demands has been made possible through recent general capital increases and the addition of a new regional development bank, the European Bank for Reconstruction and Development.

35. Net flows from IBRD and IDA (which constitute World Bank Group flows to public and publicly guaranteed recipients) roughly doubled to about US$8 billion in the first half of the decade and have since remained at a level of about 60 percent of total multilateral flows to developing countries. South Asia received the largest proportion of these funds with average net flows of US$1.9 billion during the 1980-91 period, followed by Latin America and the Caribbean (US$1.6 billion), Sub-Saharan Africa (US$1.5 billion), East Asia and Pacific (US$1.4 billion), Middle East and North Africa (US$ 0.4 billion), and Europe and Central Asia (US$ 0.3 billion).

Table 2. IBRD and IDA: Net Flows, 1980-91
(US$ billions)

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	Cumulative 1980-91
IBRD													
Net Flows													
All borrowers	3.1	3.9	4.9	5.5	6.0	5.1	5.3	4.3	2.5	2.7	5.2	2.5	51.0
Current Borrowers[1]	2.8	3.7	4.7	5.3	5.7	5.0	5.4	4.7	2.9	3.2	5.6	3.3	52.3
IDA													
Net Flows													
All borrowers	1.6	1.9	2.3	2.5	2.4	2.8	3.2	3.5	3.6	3.7	4.0	4.1	35.6
Current Borrowers[1/]	1.5	1.8	2.1	2.3	2.3	2.7	3.2	3.4	3.6	3.7	4.0	4.1	34.7

[1]*Current Borrowers are borrowers (currently servicing their loans) with a lending program for FY91-94.*

Source: World Bank

36. The variations in past and prospective net flows from IBRD and IDA reflect a number of factors. First, the maturing institution character of the Bank and IDA, resulting in high current repayments of principal arising from substantial lending in the past. Second, in a few instances, limitations on the growth in new lending arising from loan portfolio limits. Third, the recent appearance of a number of new prospective borrowers, notably in Eastern Europe and the former Soviet Union (FSU), which makes likely an increase in prospective net flows. Marked swings in overall net flows can be caused by variations in lending to a few countries, as was the case in 1991.

37. Demand for IBRD funds has been low from countries at a mature economic stage or who were early adjusters. For non-adjusters, lending has been constrained by failure to meet policy conditionalities. For other IBRD borrowers, lending has been determined by country policy performance, the level of public and private investments, and the availability of financing from other sources, including private capital. For IDA recipients, lending has been determined by performance, including macroeconomic management and poverty alleviation. Total IDA resources contributed by donors have remained constant in real terms; the increase coming exclusively from the use of reflows.

38. Net resource flows--both lending and equity investment--from the IFC are small but have been on the rise, especially since 1985. Average net flows were less than US$0.2 billion per year for the first half of the 1980s, but increased to almost US$1 billion in recent years. IFC financing has played a major catalytic role in utilizing associated private finance: for every dollar of IFC financing, other sources have contributed about five dollars. The mobilization function has expanded in the second half of the 1980s to cover portfolio investors associated with the IFC's operations in support of capital market development in the developing countries.

Table 3. IMF: Purchases Under the General Resources Account (GRA) and Disbursements Under SAF/ESAF, 1980-1991
(US$ billions)

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	Cumulative 1980-91
GRA													
Purchases	4.9	8.3	9.7	13.1	7.4	4.0	4.6	4.3	3.5	4.5	5.8	10.1	80.2
Net Purchases	0.7	5.9	7.9	11.0	5.0	0.3	-2.1	-5.9	-5.5	-3.1	-2.2	3.7	15.7
Trust Fund, SAF/ESAF													
Disbursements	1.5	0.4	0.0	0.0	0.0	0.0	0.1	0.5	0.6	1.2	0.7	1.1	6.1
Net Disbursements	1.5	0.4	-0.0	-0.0	-0.1	-0.3	-0.5	-0.1	-0.0	0.8	0.3	1.0	3.0

Source: IMF

39. Except for concessional lending from its Structural Adjustment Facility (SAF) and the Enhanced Structural Adjustment Facility (ESAF), IMF transactions with developing countries shown in Table 3 above are not included in the aggregate flow numbers presented in Annex Tables A1-A4. This is due to the special monetary nature of Fund resources and the revolving credit aspect of Fund operations. In recent years, overall purchases from the Fund have been rising as the Fund extended assistance to a larger number of countries, including in Eastern Europe. Commitments from the General Resources Account (GRA) totalled US$30.4 billion in 1989-91, while purchases reached US$20.4 billion in the same period; net flows from the Fund's GRA were a positive US$3.7 billion in 1991. This level of assistance is equivalent to about 40 percent of total multilateral nonconcessional net flows to developing countries in 1991. Prospects are for a continued high level of use of Fund resources over the next few years, in support of strong reforms and on account of the significant number of new Fund members--including the states of the former Soviet Union.

40. Net disbursements from other multilateral institutions increased significantly over the last decade. The combined net flows from the Asian Development Bank (AsDB) and the Asian Development Fund reached an estimated US$2.3 billion in 1991, more than four times larger than in 1980. The African Development Bank (AfDB), along with the African Development Fund, provided rapidly increasing net flows, especially in the latter half of 1980s, which exceeded US$1.8 billion in 1991. After several years of a declining lending volume since the mid-1980s, net flows from the Inter-American Development Bank (IDB) rebounded to an estimated US$1.3 billion in 1991.[7]

41. The European Bank for Reconstruction and Development (EBRD) was established in April 1991 to foster the transition towards open market economies and to promote private and entrepreneurial initiative in the Central and Eastern European countries. During its first year of operation, the EBRD

[7] *Other sources of multilateral flows include the Arab Fund and the Islamic Development Bank.*

approved loans and investments in equities totalling approximately US$600 million equivalent (although none was disbursed in 1991).

42. **Concessional Flows (ODA).** Bilateral and multilateral ODA has supported developing countries in meeting investment requirements for sustained growth, for the reduction of poverty, and for the protection of the environment. Total ODA flows now account for more than 40 percent of all flows to developing countries, up from one quarter in 1982. ODA flows have grown steadily, about 3 percent per year in nominal terms, since 1982 (Annex Table A5).[8] In real terms, however, growth has been zero and ODA flows have fallen as a share of donor economies over the past decade, to 0.34 percent of GNP compared with the 0.7 percent target. Relative to per capita incomes of recipient countries, ODA flows have fallen in real terms.

43. IDA remains the largest multilateral concessional lender, accounting for more than 60 percent of multilateral concessional credits to developing countries.[9] Other major sources of multilateral concessional loans and grants include the IMF through the SAF and ESAF, U.N. agencies, the European Community, and the concessional windows of the three major regional development banks. The European Community and the Asian Development Fund have been the fastest growing sources of multilateral concessional development funds since 1982. About two thirds of recent net flows to Sub-Saharan Africa have gone to countries eligible for the World Bank's Special Program of Assistance (SPA) which coordinates donor flows to Sub-Saharan African countries undertaking adjustment programs. Aggregate net flows to SPA countries rose to US$7 billion per year during the first SPA program (1988-90) from US$5.5 billion per year in the previous three years. Since 1986, net disbursements from IDA to all developing countries have averaged US$3.8 billion per annum, or nearly US$19 billion over the period 1987-91. Since 1986, the Fund has committed over US$5 billion of concessional lending at an annual interest rate of 0.5 percent under the SAF/ESAF to low-income countries. Of this amount, over US$4 billion has been disbursed; allowing for repayments of earlier Trust Fund loans over this period, net disbursements totalled nearly US$3 billion. Around two thirds of this lending was to Africa with most of the remainder to South Asia.

44. Despite the continued importance of multilateral concessional lending, nearly all of the increase in development assistance from member countries of the OECD Development Assistance Committee (DAC) in recent years has been channelled through bilateral aid programs. ODA budgetary allocations for multilateral institutions from DAC countries remained roughly constant throughout the 1980s.

45. Grants, which made up 55 percent of total bilateral ODA flows in 1981, now make up two thirds of these flows. The source-country composition of bilateral ODA flows shifted during the decade. Declines in ODA flows from capital surplus oil exporters and Central and Eastern European countries were more than offset by increases in ODA from DAC countries. ODA from Arab countries declined

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[8] *Figures for ODA flows have been adjusted to exclude debt forgiveness, which was substantial in 1990 and 1991.*

[9] *A progress report on the status of the current IDA replenishment negotiations is included in the President's Report to the Development Committee.*

from US$10 billion in 1981 to US$2 billion in 1989 but rose to more than US$6 billion in 1990; in 1991, however, the figure is estimated to be much smaller than in 1990. In spite of the declines, ODA from these countries continued to represent well above 0.7 percent of GNP, and stood at several times that level throughout the 1970s. ODA from Central and Eastern European countries reached US$5 billion in 1987 but declined to US$2 billion in 1990 and was probably lower in 1991. ODA flows from other developing country donors remain insignificant.

IV. IMPROVING DEVELOPING COUNTRY ACCESS TO EXTERNAL FINANCE

A. Overall Outlook for Development Finance

46. The prospects for sustaining the recent increases in net ODA flows are poor, given budgetary difficulties in several major donor countries, notwithstanding reductions in military expenditures. New claimants for official support, from Eastern Europe and Central Asia, will put further pressure on ODA budgets.[10] ODA flows from capital surplus countries in the Middle East are likely to decline further, as they face reconstruction costs and the aftermath of exceptional spending in connection with the Gulf war. Substantial efforts, therefore, are necessary from both the donor and recipient countries to achieve a more efficient use of available resources and thereby enhance the effectiveness of aid.

47. Based on current trends and on the assumption of strong adjustment policies in developing countries, external financial flows likely to be available correspond to modest current account deficits. A very large part of developing country investments will continue to be financed by domestic savings. An increasing number of middle-income countries will be able to attract substantial commercial external financing on a sustainable basis, based on a combination of strong adjustment efforts, a more conducive climate for FDI and other external private investments. However, initially, some adjusting countries will continue to face constraints in access to private flows until confidence is fully restored, and they will therefore require support from official financing sources.

48. In the poorest countries, the need for external financing will be larger as more countries embark on market-oriented reforms, pursue poverty reduction, and address environmental concerns. Adequate concessional financing from both bilateral and multilateral sources will continue to play a critical role in establishing the conditions for sustainable growth. This will need to be supplemented by continued efforts to improve the quality of assistance, for example by untying aid and simplifying donor and recipient procedures. A slowdown in ODA growth or diversion of ODA resources to middle-income countries would adversely affect the ability of the poorest countries to maintain the necessary adjustment programs. The statement of the July 1992 G7 Summit is, therefore, to be welcomed that "We shall direct official development assistance more towards the poorest countries."

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[10] *According to the current DAC guidelines, grants and loans at concessional terms to certain countries in Eastern Europe are not recorded in the ODA statistics. Arrangements have been made, however, for the OECD Secretariat to collect data on these financial flows, including official aid.*

B. Developing Country Policies

49. Countries without access to international capital markets, particularly SILICs, will have to rely primarily on domestic savings, supplemented by external concessional flows. Given constraints on ODA and increasing demand on aid budgets, these countries would have to demonstrate that aid is being put to productive use. This requires sustained commitment to adjustment efforts involving appropriate macroeconomic policies--particularly improvement in public sector savings performance--and structural reforms as well as progress on issues of poverty, the environment, human resource development, and governance. For many countries, policies to attract FDI and other equity flows would also play a key role in both providing finance and stimulating growth: the share of private investment in developing countries that is financed by FDI has risen from a low of about 4 percent in 1984 to about 10 percent in 1990.

50. Middle-income countries implementing policies to resume growth and restore creditworthiness will face a wider choice of external financing opportunities in the 1990s than in the preceding decade. The supply of private external finance is becoming more differentiated by borrower creditworthiness in respect of not only volume, but also cost and type of investment. For long-term investment, traditional bank financing is likely to be largely replaced by non-bank sources. Access to bond markets, FDI, portfolio equity flows, and bank lending will hinge critically on a developing country's economic performance and policy reforms. Beyond general macroeconomic stability and growth, developing country governments may consider a number of actions that could foster improved confidence in the domestic private sector, liberalize the financial sector, and progressively dismantle barriers to direct investment and portfolio equity flows.

51. Developing countries typically place a variety of controls on FDI by non-residents.[11] These controls may incur a high cost not only in financing foregone (which will extend beyond FDI to other financing flows), but also in the loss of the concomitant flows of technology and know-how. While in no way a panacea, access to FDI is a key factor in development. Developing country policymakers should review such areas as institutional procedures for approval of new investment, rules for repatriation of capital and profits (including the exchange control regime), limitations on the proportion of foreign equity, local content requirements, the effectiveness of tax incentives, accounting standards, and legal protections, with a view to improving FDI flows.

52. More specifically, policymakers may wish to consider permitting free admission of foreign investment as the general rule; defining clearly the types of investment activities that will garner incentives; not favoring foreign over local investors in granting incentives; not using tax holidays; permitting unrestricted transfers abroad of dividends, capital, royalties, and interest payments; not placing restrictions on investors' access to foreign exchange; not undertaking expensive investment promotions; and establishing an investment promotion agency with close ties to the local private sector and a focus

[11] *"Issues Paper on "The Role of Foreign Direct Investment in Development," dated April 14, 1991, DC/91/5.*

on investor support rather than on screening.

53. Similar remarks apply to regulatory restrictions on portfolio equity flows. The existence of strong capital markets helps to attract external private investment. Carefully structured prudential, supervisory and accounting regulations can contribute to the confidence of both domestic and foreign investors. Examples include the application of clear disclosure and accounting standards for firms, capital adequacy standards for financial institutions, and prohibitions on insider dealing in financial markets. More generally, repression of the domestic financial sector (for instance, through interest rate controls and directed credit) can lead to distortions that result in unwelcome outflows.

C. Industrial Country Policies

54. Industrial country policies also affect developing country access to external finance. Global interest rates are largely determined by savings and investment in industrial countries, and directly influence terms of new lending and cost of servicing existing (variable rate) debt. Measures to reduce fiscal deficits in some major industrial countries (including the reduction of military expenditures where justified by recent world developments) would improve prospects for resource flows to developing countries; longer-term measures to improve personal sector saving would also be desirable. Progress towards a more open trading system in the Uruguay Round is also crucial, given the high costs of protection[12], in determining the profitability of potential investment, including FDI, and influencing the growth prospects of developing countries.

55. Industrial country policy concerning ODA flows will have a direct impact on the access of the poorest countries to other forms of external finance. While many ODA recipient countries have good long-term growth prospects, the risks they pose to external investors are too great, at early stages, to attract large amounts of private external finance. Existing ODA resources can be used most efficiently if they are concentrated on the countries with the greatest need and on countries with the policies to make the most effective use of external resources. Of central importance in this context are the adoption of sound programs of poverty reduction. Lending by multilateral institutions, particularly on concessional terms, and coordination such as the SPA and consultative groups, can help ensure the most effective use of scarce resources. However, as more developing countries adopt reform programs and pursue poverty-oriented strategies, the need for ODA is increasing. The increase of aid budgets is critical to generate the resources necessary to support this adjustment, particularly in an environment where traditional ODA recipients have to compete with new claimants for official aid. While there is no clear evidence as yet of aid diversion or aid reduction as a result of new official flows to Eastern Europe and Central Asia, the potential for diversion is a valid concern for the future. Unless aid budgets are increased to cover grant financing and concessional loans (other than food aid), other ODA recipients will be affected adversely.

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[12] *The cost of protection in welfare and export earnings foregone are dealt with in the Progress Report on Trade Policy Developments.*

56. Industrial countries also have a role to play in encouraging outward FDI, through taxation and other bilateral agreements (e.g. tax sparing and double taxation agreements), and through institutional arrangements that provide investment guarantees, technical assistance, and the provision of information. And support for export credits can play a vital role in ensuring adequate financing for imports in the context of reform efforts.

57. Industrial country policies on prudential supervision of banks may also influence financial flows to developing countries, although these regulatory requirements have not so far played a major role in determining developing country access to external financial markets. Industrial country regulatory authorities should review capital adequacy and provisioning standards to assess whether they provide sufficient flexibility to reflect the improvement in creditworthiness achieved by a number of countries.

V. ROLE OF OFFICIAL MULTILATERAL INSTITUTIONS

58. Multilateral institutions have an important role to play, not only in the direct provision of external finance for development, but in catalyzing and coordinating other official and private flows. In this context continued close cooperation between the Fund and the Bank will be essential. The main role of the Fund is to promote a supportive global economic environment through its surveillance role, with policy advice for industrial and developing countries. Additionally, the Fund provides financial and technical assistance for structural adjustment efforts of its members, with particular emphasis on macroeconomic policies and, together with the Bank, on key structural measures. Concessional lending under the SAF and ESAF facilities has played a key role in supporting reform efforts of low-income countries while policy framework papers (PFPs) agreed with national authorities and the Bank have provided helpful guidelines for bilateral/multilateral donors. Such Fund support for structural adjustment has helped to catalyze other sources of financing, including debt relief and the Paris Club and donor flows. The main role of the Bank is to help developing countries reduce poverty and achieve sustainable growth through a combination of financing, policy advice, and technical assistance. The Bank supports adjustment programs, investments in increased output and productivity, more efficient delivery of social services to more people, and an incentive framework which promotes efficiency, private savings, and investment. The Bank also plays an important role in catalyzing private flows, partly through its program of co-financing. Concessional lending under IDA together with co-financing and coordinated financing (e.g. through SPA) continues to play a central role in the adjustment programs of low-income countries. Moreover, IDA, which has a proven record of developmental effectiveness, has been requested to shoulder additional responsibilities, including enhanced support for poverty reduction and environmental protection. To meet these additional responsibilities, will require a significant increase in real terms over IDA-9 in the replenishment of IDA-10.

59. A growing share of investment demand will come from the private sector as more economies become market oriented, the business environment improves, and more governments rely on the savings and entrepreneurial skills of their citizens to increase productivity and output. MIGA and source-country guarantee programs can facilitate direct investment. An expanded IFC, through investment operations,

will continue to support private sectors in developing countries. IFC plays an important catalytic role, partially through loan syndications. The Foreign Investment Advisory Service (FIAS), joint facility of IFC and MIGA, helps governments to adjust policies, institutions, and programs that affect FDI. Regional development banks also have private sector financing facilities. In addition, some multilateral institutions will continue to provide direct support to privatization programs and are exploring new ways of providing support to private sector firms in developing countries.

Appendix I. Aggregate Net Flows and Net Transfers

Each year developing countries receive external capital inflows in the form of loan disbursements. These loans help finance investment and imports in support of economic development. Developing countries make amortization payments on loans they received in previous years. The difference is reported here as debt-related net flows. These net flows will equal the increase in a country's external indebtedness, aside from debt forgiveness (and in the absence of exchange rate changes). A normal pattern would be positive net debt flows to a country at an early stage of development (a debt build-up), declining net flows as a country achieves a more advanced stage of development (debt stabilization), followed by capital exports at a high level of development (resulting eventually in a net creditor status).

The concept of net debt flows can be broadened to include other sources of external financing of development. The aggregate net flows concept used here includes grants and FDI. Grants do not generate future repayment obligations, and have a strictly positive impact on net flows. FDI is included on a net basis, gross inflows (including reinvested profits) minus the repatriation of earlier FDI capital. Aggregate net flows correspond to the financing of the current account deficit plus changes in reserves (plus any private capital outflows generated by domestic residents; these outflows have been large in some countries).

Debt and FDI generate obligations. Interest payments represent compensation to creditors for the use of resources. If the resources have been invested productively, the return generated should more than cover the interest cost. Foreign investors expect compensation in the form of profit remittances, which are more directly related to profitability of the investment activity. In general, effective use of external resources should generate the capacity to meet these external obligations. Aggregate net transfers are calculated by subtracting interest payments and profit remittances from aggregate net flows.

Just as aggregate net flows correspond to the current account, aggregate net transfers correspond to the trade balance (more exactly, to the non-interest current account balance). This concept must be used with caution. As implied above, net transfers is an incomplete account of the benefits of a capital inflow, since the incremental output generated by the corresponding investment is not captured. Unless aggregate net flows to a country are in the form of grants or highly concessional loans, maintaining positive net transfers will cause a rapid rise in external indebtedness: the debt stock would rise at a compound rate that exceeds the rate of interest on the debt. Whatever the terms, therefore, positive net transfers on debt-related transactions is inconsistent with a reduction in debt stocks (abstracting from outright forgiveness). Furthermore, positive net transfers and the implied rapid growth in debt will not be sustainable unless accompanied by equally rapid growth in the debtor's output and exports.

Aggregate net transfers for a group of countries can be misleading. Some countries in the grouping may be at a more mature development stage, in which net flows are small and net transfers, particularly net debt transfers, would be expected to be negative. Others may have acquired levels of

debt that are inconsistent with growth prospects. Still others may be at a level of development in which external borrowing is growing and positive net transfers would be normal. Very poor countries with weak growth prospects may be maintaining positive net transfers through concessional official development assistance. Hence, the aggregate net transfer to the group is almost certain to be a poor guide to the external financing position of any individual country in the group.

The above analysis considers net transfers from the point of view of a debtor country. The concept also must be used with considerable caution when applied to an individual creditor. If a financial institution is maintaining positive net transfers, its asset base is growing rapidly. Prudence would require that its equity capital base grow equally as rapidly. For example, if a bank were to make one loan of US$100 in 1992, in order to maintain even small positive net transfers at an interest rate of 9 percent, its outstanding assets would be at least US$200 by 2000. Thus, its capital base would also need to double, at a minimum. An individual creditor institution will tend to maintain positive net transfers to newer borrowers or to creditworthy borrowers with unanticipated short-or medium-term liquidity needs and negative net transfers but positive net flows to mature borrowers. Hence, the overall position of a creditor institution with respect to its net transfers will depend, among other factors, on its past lending and the rate of growth of its equity capital base.

Appendix II. Data Coverage by Groups of Developing Countries

The country coverage of the Annex tables is as shown below.

Geographic Groups

Africa, South of the Sahara

Angola
Benin
Botswana
Burkina Faso
Burundi
Cameroon
Cape Verde
Central African Republic
Chad
Comoros
Congo, Republic of
Cote d'Ivoire
Djibouti
Equatorial Guinea
Ethiopia
Gabon
Gambia, The
Ghana
Guinea
Guinea-Bissau
Kenya
Lesotho
Liberia
Madagascar
Malawi
Mali
Mauritania
Mauritius
Mozambique
Niger
Nigeria
Rwanda
Sao Tome and Principe
Senegal
Seychelles
Sierra Leone
Somalia
Sudan
Swaziland
Tanzania
Togo
Uganda
Zaire
Zambia
Zimbabwe

East Asia and the Pacific

China
Fiji
Indonesia
Korea, Republic of
Lao People's Democratic Republic
Malaysia
Papua New Guinea
Philippines
Solomon Islands
Thailand
Tonga
Vanuatu
Western Samoa

Europe and the Mediterranean

Bulgaria
Cyprus
Czechoslovakia
Hungary
Malta
Poland
Portugal
Romania
Turkey
Yugoslavia

Latin America and the Caribbean

Argentina
Belize
Bolivia
Brazil
Chile
Colombia
Costa Rica
Dominica
Dominican Republic
Ecuador
El Salvador
Grenada
Guatemala
Guyana
Haiti
Honduras
Jamaica
Mexico
Nicaragua
Panama
Paraguay
Peru
St. Kitts and Nevis
St. Lucia
St. Vincent
Trinidad and Tobago
Uruguay
Venezuela

North Africa and the Middle East

Algeria
Egypt, Arab Republic of
Iran, Republic Islamic of
Jordan
Lebanon
Morocco
Oman
Syrian Arab Republic
Tunisia
Yemen, Republic of

South Asia

Bangladesh
Bhutan
India
Maldives
Myanmar
Nepal
Pakistan
Sri Lanka

Appendix III. Recent Trends in External Finance For Developing Countries[13]

The last decade has witnessed fundamental changes in the pattern of resource flows to developing countries. Aggregate net flows (in real terms) dropped precipitously from the peak of US$125 billion in 1981 to a trough of US$63 billion in 1987, mainly because the debt crisis caused commercial bank lending to diminish abruptly. Since 1987, net flows have rebounded as a result of increasing official flows in support of adjustment programs and a reemergence of private capital flows, particularly in the form of FDI. Aggregate net transfers followed a similar trend. After being negative in the middle years of the 1980s, net transfers turned positive for the last three years.

Sub-Saharan Africa has experienced a decade of generally rising development assistance flows and declining private flows. Official development assistance (ODA) represented about half of net resource flows to Sub-Saharan Africa in 1981. By 1991, ODA with an implied grant element of over 95 percent represented an estimated 90 percent of resource flows to the region. Overall, net flows in 1991 were US$14 billion or 8 percent of GNP. Most Sub-Saharan African countries have not had access to external private financial markets in recent years, except for limited volumes of short-term trade finance. The highly concessional nature of the flows to this region resulted in an average of over US$7 billion a year positive net transfers over the period 1980-91.

Latin America experienced a sharp swing in current account deficits and international reserves throughout the 1980s. The loss of capital market access, following the onset of the debt crisis, resulted in a large decline in net resource inflows, from US$57 billion in 1981 to US$12 billion in 1989 and a consequent fall in current account deficits because of import compression. Since 1990, net resource flows have risen, reaching US$20 billion in 1991. The experience of this region highlights the degree to which macroeconomic performance and improvements in the investment climate can attract both private and official flows.

In contrast to Sub-Saharan Africa, net transfers to Latin America have been negative since early in the debt crisis. While principal payments on commercial bank debt were often rescheduled, debtor countries were able to refinance only a relatively small share of interest payments and, therefore, apart from episodes of running arrears, made large cash interest payments. Recently, negative net transfers have been small, about US$6 billion in 1991, reflecting lower interest rates and a renewal of market access in several countries.

Countries in **East Asia and the Pacific** generally experienced small current account deficits, less than two percent of GNP, throughout much of the 1980s, except for a small surplus in 1987 and 1988. With improved export performance and availability of external finance, they were able to build up reserves at an average rate of almost US$6 billion per year.

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[13] *The countries included in each of the regions, as used in this paper, are shown in Appendix II. The net flows data used in this paper exclude interest rescheduled, interest arrears, and debt reduction and forgiveness.*

Net resource flows to this region declined largely as a result of a decline in demand. Several countries in the region retired significant amounts of debt, some of it before maturity, notably in 1987. Concessional flows remained very small. However, in this region, too, the current sources of external finance are different from those of the early 1980s. FDI accounted for nearly 40 percent of net flows in 1991, compared with less than 15 percent in 1981. Official nonconcessional loans have become a major financing source, accounting for 40 percent of debt flows and almost 20 percent of aggregate flows in recent years. The changing pattern of sources of external finance reflects the general macroeconomic stability and the high credit standing of East Asian countries, both of which contributed to an attractive climate for FDI.

South Asia experienced generally rising current account deficits between 1981 and 1991. The aggregate deficit for this group of countries was US$13 billion in 1991, about 3 percent of GNP. The composition of net resource flows to South Asia was much more stable than in other geographical regions. ODA accounted for at least 60 percent of net resource flows in every year. Commercial bank and bond flows rose marginally in the 1980s but by 1991 were lower in real terms than in 1981. FDI in this region has remained small throughout the decade, never exceeding 4 percent of net flows. Net transfers were consistently positive and roughly constant in real terms.

Europe and Central Asia consists of three distinct groups: the formerly centrally-planned countries of Eastern Europe, the market-economy developing countries of Europe and the countries of the former Soviet Union (FSU). The three groups of countries experienced distinct patterns of current account balance and access to external finance between 1980 and 1991.

The Eastern European countries as a group moved from current account deficit in 1981 to current account surplus through most of the 1980s and back to deficit in 1990 and 1991. Aggregate net resource flows declined sharply and turned negative in 1987 and 1988. A modest rebound in net flows has been recorded since then, reaching almost US$1 billion in 1991. Net transfers, however, have remained consistently and substantially negative since the onset of the debt crisis in 1982. The picture for net transfers to Eastern Europe has thus been similar to, and has dominated, that for Europe and the Mediterranean as a whole, i.e. excluding the FSU.

The other European countries (a heterogenous group consisting of Turkey, Malta, Portugal, and Cyprus) reduced their current account deficit from 1981 on and turned to a surplus in 1990. A sharp drop in exports in 1991, however, led to a current account deficit of almost US$5 billion in 1991. International reserves were largely stable until 1988. A substantial reserves build-up in 1989 and 1990 was more than offset by a huge reduction in reserves in 1991, in the wake of the Gulf War. Net resource flows have been consistently positive with relatively small yearly variations. Net transfers have fluctuated in a range of -US$2 billion to US$2 billion.

The FSU experienced current account surpluses up to 1988 and deficits thereafter. Reserve transactions were minimal, except for 1990 when two thirds of the US$21 billion current account deficit was financed from reserves. In spite of current account surpluses, net resource flows were positive in years preceding 1988 as large increases in long-term borrowing from official sources offset sharp drops.

in net borrowing from commercial banks.[14]

The capital importing countries of the **Middle East and North Africa** moved from an aggregate current account deficit of about 4 percent of GNP to a surplus of about 1 percent of GNP during the last decade. Official reserves at end-1991 were about US$8 billion lower than at the end of 1981.

The movement in the current account from deficit to surplus reflected in part reduced access to external flows; consequently, net transfers have become negative. Recently, net flows from private creditors have also been negative, partially offset by small positive net flows from official creditors. ODA flows have accounted for about two thirds of total flows. Multilateral nonconcessional lending is the only component of external flows that has increased in recent years.

Severely Indebted Countries.[15] When developing countries are grouped by degrees of indebtedness, net resource flows to severely indebted low-income countries (SILICs) have risen over the last decade thanks to growth in official concessional flows. Aggregate real net flows averaged roughly US$15 billion per year during the 1980-91 period, which was used to finance current account deficits of almost US$10 billion, including substantial debt servicing costs. Net transfers to SILICs have been consistently positive and have grown to US$12 billion in 1991. The pattern of net flows and transfers to low-income countries as a whole has been similar to that for the SILICs, but of about twice the size.

Net resource flows to severely indebted middle-income countries (SIMICs) generally declined through 1989. Net flows have rebounded since then and reached US$16 billion in 1991, owing to rapidly increased bond issues (particularly by Latin American borrowers). Since the debt crisis in 1982, net transfers to SIMICs have remained strongly negative, reaching -US$10 billion in 1990 and -US$13 billion in 1991, which however was less negative than in earlier years.

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[14] *Macroeconomic data for the FSU are taken from the IMF's World Economic Outlook (WEO), May 1992. The annex tables on resource flows do not include the FSU figures because of lack of comparable data on a long-run historical basis.*

[15] *As in the World Debt Tables, a country is classified as severely indebted if any three of four debt indicators, calculated on a three-year average, are above critical values: a debt-to-GNP ratio of 50 percent, a debt-to-export ratio of 275 percent, a ratio of scheduled debt service to exports of 30 percent, and a ratio of scheduled interest payments to exports of 20 percent.*

TABLE A1. Aggregate Net Resource Flows (Long-Term), by Source, 1980-1991

	NOMINAL (US$ billions)						REAL (Constant 1991 US$ billions)				
	Aggregate Net Res. Flows	Official Grants	Official Loans	Private Loans	FDI	Import Unit Value Index[1]	Aggregate Net Res. Flows	Official Grants	Official Loans	Private Loans	FDI
1980	84.4	12.6	21.1	41.5	9.2	81.3	103.8	15.5	25.9	51.1	11.4
1981	101.6	11.4	23.8	53.4	12.9	81.3	125.0	14.1	29.2	65.7	15.9
1982	91.0	10.5	24.8	44.6	11.1	82.2	110.8	12.7	30.2	54.3	13.5
1983	72.1	10.0	24.0	29.4	8.7	79.8	90.3	12.5	30.1	36.9	10.8
1984	63.5	11.5	22.0	21.6	8.4	78.6	80.7	14.6	28.0	27.5	10.7
1985	60.5	13.3	21.0	15.7	10.6	76.6	79.0	17.3	27.4	20.4	13.9
1986	55.0	14.1	22.1	9.2	9.6	77.5	70.9	18.2	28.5	11.9	12.3
1987	51.7	14.9	21.0	2.3	13.5	82.3	62.8	18.1	25.5	2.8	16.4
1988	66.0	17.4	19.3	9.8	19.6	87.1	75.8	20.0	22.1	11.2	22.5
1989	70.5	18.1	21.1	7.6	23.6	89.7	78.6	20.2	23.6	8.4	26.3
1990	76.3	21.4	22.8	7.2	25.2	96.4	79.1	22.2	23.6	7.4	26.1
1991	81.7	19.8	25.5	12.2	24.1	100.0	81.7	19.8	25.5	12.2	24.1

Source: World Bank, IMF

[1]The import unit value index, produced by the IMF (World Economic Outlook database), is weighted by the US dollar value of each developing country's imports.

TABLE A2. Aggregate Real Net Resource Flows (Long-Term) by Region and Income Groups, 1980-1991
(Constant 1991 US$ billions)

		GEOGRAPHIC REGIONS						SELECTED INCOME GROUPS			
	Aggregate	S.S. Africa	South Asia	East Asia	Latin America & the Caribbean	N. Africa & M. East	Europe & The Med.	SPA Countries	SILIC	SIMIC	Low Inc. Countries
1980	103.8	13.6	7.2	15.2	36.3	14.3	15.0	6.1	12.8	40.7	25.7
1981	125.0	15.2	6.8	18.6	57.3	12.9	12.1	5.4	15.3	57.3	26.4
1982	110.8	16.4	7.8	19.4	44.3	13.1	7.8	5.2	16.3	44.9	29.7
1983	90.3	13.3	6.3	23.5	25.7	13.3	6.3	5.1	13.9	25.4	28.6
1984	80.7	11.7	8.1	20.7	21.9	9.7	6.0	6.0	12.1	20.0	28.1
1985	79.0	12.3	7.7	21.0	17.4	12.7	5.0	5.7	12.7	17.1	31.2
1986	70.9	13.9	9.5	13.9	12.8	13.6	4.6	7.5	14.2	14.5	36.4
1987	62.8	16.0	9.8	5.3	15.4	11.9	1.0	7.7	15.1	19.0	40.2
1988	75.8	14.8	10.6	15.1	15.8	9.4	4.8	7.7	14.1	17.9	41.3
1989	78.6	18.1	11.8	22.0	12.0	7.9	6.7	8.0	14.9	9.1	42.1
1990	79.1	15.8	9.0	25.5	19.3	4.4	5.1	9.7	17.1	17.0	44.5
1991	81.7	14.4	10.4	27.0	19.7	6.8	3.4	6.9	16.7	15.8	38.4

Source: World Bank, IMF

TABLE A3. Aggregate Net Transfers (Long-Term), by Source, 1980-1991

	NOMINAL (US$billions)						REAL (Constant 1991 US$ billions)				
	Aggregate	Official Grants	Official Loans	Private Loans	FDI	Import Unit Value Index[1]	Aggregate	Official Grants	Official Loans	Private Loans	FDI
1980	37.6	12.6	15.1	15.1	(5.2)	81.3	46.3	15.5	18.6	18.6	(6.4)
1981	46.4	11.4	17.0	19.8	(1.8)	81.3	57.1	14.1	21.0	24.3	(2.3)
1982	29.2	10.5	17.4	4.6	(3.2)	82.2	35.6	12.7	21.2	5.5	(3.9)
1983	13.7	10.0	15.7	(8.9)	(3.1)	79.8	17.2	12.5	19.7	(11.1)	(3.9)
1984	(0.2)	11.5	12.6	(22.0)	(2.2)	78.6	(0.2)	14.6	16.0	(28.0)	(2.8)
1985	(4.5)	13.3	9.6	(27.3)	(0.2)	76.6	(5.9)	17.3	12.6	(35.6)	(0.2)
1986	(7.3)	14.1	8.2	(29.2)	(0.4)	77.5	(9.4)	18.2	10.5	(37.6)	(0.5)
1987	(12.4)	14.9	5.8	(35.5)	2.3	82.3	(15.1)	18.1	7.1	(43.1)	2.8
1988	(6.5)	17.4	2.2	(33.7)	7.6	87.1	(7.4)	20.0	2.5	(38.7)	8.7
1989	3.2	18.1	4.2	(29.3)	10.2	89.7	3.5	20.2	4.6	(32.7)	11.4
1990	10.9	21.4	4.2	(25.8)	11.1	96.4	11.3	22.2	4.3	(26.8)	11.5
1991	13.5	19.8	4.4	(22.8)	12.1	100.0	13.5	19.8	4.4	(22.8)	12.1

Source: World Bank, IMF.

[1] The import unit value index, produced by the IMF (World Economic Outlook database), is weighted by the US dollar value of each developing country's imports.

TABLE A4. Aggregate Real Net Transfers (Long-Term), by Region and Income Groups, 1980-1991
(Constant 1991 US$ billions)

		GEOGRAPHIC REGIONS						SELECTED INCOME GROUPS			
	Aggregate	S. S. Africa	South Asia	East Asia	Latin America & the Caribbean	North Africa & Middle East	Europe & the Middle East	SPA Countries	Silics	Simics	Low Income Countries
1980	46.3	7.3	5.9	3.4	8.9	8.2	10.2	4.8	7.9	12.8	13.8
1981	57.1	9.9	5.4	4.3	22.9	6.8	5.8	4.4	10.9	23.0	13.7
1982	35.6	11.1	6.2	4.3	4.3	7.1	0.6	4.1	12.2	5.6	16.7
1983	17.2	8.2	4.3	7.8	(11.5)	7.4	(1.0)	4.0	9.6	(10.7)	15.2
1984	(0.2)	6.1	5.9	4.3	(19.7)	3.9	(3.2)	5.0	7.5	(20.1)	14.4
1985	(5.9)	5.8	4.8	4.4	(25.7)	6.6	(4.9)	4.6	7.2	(25.1)	16.8
1986	(9.4)	8.5	6.0	(2.1)	(26.1)	6.9	(5.4)	6.3	10.1	(23.5)	23.1
1987	(15.1)	10.2	5.9	(10.9)	(20.5)	6.0	(9.0)	6.1	10.7	(16.2)	26.0
1988	(7.4)	8.9	6.3	(1.6)	(24.0)	2.7	(5.0)	6.2	9.2	(22.2)	25.5
1989	3.5	13.2	7.2	4.1	(19.0)	1.1	(3.0)	6.7	10.4	(21.3)	25.0
1990	11.3	10.9	4.2	8.4	(6.5)	(1.5)	(3.8)	8.7	12.7	(10.0)	27.6
1991	13.5	9.5	5.8	8.1	(8.1)	1.7	(5.4)	5.8	11.7	(13.4)	21.8

Source: World Bank, IMF.

TABLE A5. Official Concessional Flows to Developing Countries by Types of Flows; 1980-91
(US$ billions)

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991E
Official Development Assistance	23.5	24.1	22.5	21.4	20.4	24.3	26.1	30.6	30.9	33.2	36.3	34.1
Bilateral Loans	8.2	9.4	8.3	7.9	5.2	7.0	7.4	10.2	8.1	9.7	8.6	8.0
Multilateral Loans	2.7	3.3	3.7	3.5	3.7	4.0	4.6	5.5	5.4	5.4	6.3	6.3
Official Grants[1]	12.6	11.4	10.5	10.0	11.5	13.3	14.1	14.9	17.4	18.1	21.4	19.8
Memorandum Items:												
ODA in real terms[2]	28.9	29.7	27.3	26.8	25.9	31.7	33.7	37.2	35.5	37.1	37.7	34.1
ODA in real terms[3]	38.0	41.0	39.3	37.7	36.9	43.6	37.1	37.6	35.3	38.5	37.6	34.1

Source: OECD, World Bank, IMF.

[1]Excludes Technical Cooperation Grants, and estimated debt forgiveness.
[2]Based on import unit value index (Source: IMF, WEO)
[3]Based on OECD GNP deflator
E denotes estimated figures

LEGAL FRAMEWORK FOR THE TREATMENT OF FOREIGN INVESTMENT

REPORT TO THE DEVELOPMENT COMMITTEE

September 1992

INTRODUCTORY REMARKS

1. This report is prepared in response to the Development Committee's request, made in its Spring 1991 meeting at the initiative of France, for a report on "an overall legal framework which would embody the essential legal principles so as to promote FDI." It follows a progress report submitted to the Committee in its Spring 1992 meeting which described the approach to be followed and its rationale and outlined the scope of coverage of the proposed framework.

2. The work reflected in this report differs from the task being undertaken since 1977 by the UN Centre on Transnational Corporations (UNCTC) in at least two respects. First, this report covers general principles suggested to guide governmental behavior toward foreign investors; it does not include rules of good conduct on the part of the foreign investors. A set of rules for the latter purpose was reflected in negotiated provisions of the UNCTC draft Code of Conduct, which is now being reviewed "in the light of the changed international economic environment."[1] As previously prepared, "[t]hese provisions shared the common goal of maximizing the contributions of TNCs [transnational corporations] to the economic and social development of the countries in which they operate, and minimizing their potential negative effect."[2] They specifically relate to disclosure of information by foreign corporations, environmental and consumer protection, restrictive business practices, the avoidance of corrupt practices and transfer pricing, parent-affiliate relations as well as labor relations and working conditions. While the framework covered by this report avoids a repetition of these principles, the proposed guidelines are meant to apply to bona fide private investments, where investors act in good faith and in full conformity with the laws and regulations of the host State.[3] They also provide that restrictions applicable to national investment on account of public order, public health and the protection of the environment will equally apply to foreign investment.[4] Furthermore, the proposed framework includes a recommendation for all States to take appropriate measures for the prevention and control of corrupt business practices and the promotion of accountability and transparency in dealings with foreign investors and to cooperate with other States in developing international procedures and mechanisms to this effect.[5]

3. Second, this report does not aim at representing a codification of what are necessarily agreed upon, binding rules of international law. Rather, it attempts to reflect

at this stage generally acceptable international standards which meet the objective stated in the Development Committee's request, i.e., the promotion of foreign direct investment. Fortunately, any gap that may exist between principles which are widely accepted as legally binding international law and the guidelines proposed in this report is narrowing as a result of the changing realities and perceptions related to the policy environment for foreign investment in practically all developing countries and the intensified normative activity in this field in recent years, at both the regional and global levels. It is recognized, however, that some of the standards prepared here, though not the ultimate that the world community may aspire to, do reflect emerging, rather than settled, standards under contemporary international law and for this reason represent in several respects what is deemed to be desirable, rather than common practice. As they are meant to provide the elements of an international framework which may develop in the future into generally accepted standards, the proposed guidelines should not also be read as the ultimate recommended policy for every country interested in attracting foreign investment. The conditions of a specific country may well require it to adopt a more liberal approach, which is justified by its circumstances, than what are deemed to be internationally acceptable standards at this stage.

4. The attempt to formulate generally acceptable international standards to promote the flow of foreign investment is both timely and useful. It is timely because of the growing importance of private direct foreign investment in developing countries. Such flows have increased substantially, reaching in 1991 a level almost three times higher than that of 1986[6] and accounting at present for about ten percent of all private investment in the developing countries.[7] They also hold a significant potential for further growth in the 1990s, compared to the expected modest growth in official assistance and commercial lending.[8] This work is also timely because of the great transformation of economies in Eastern Europe, Central Asia and indeed many developing countries, from inward looking economies, based on public sector control and inspired by import substitution policies, into outward looking market economies, based on private sector development and open competition. In conjunction with this transformation, such events as nationalizations of foreign investments are becoming increasingly rare and, with changing patterns of foreign investment flows, traditional classifications of and distinctions between "home" and "host" countries have lost some of their significance, suggesting in turn a more balanced approach to foreign investment issues.[9]

5. This transformation process and the general trend to attract foreign investment make it particularly useful to try to devise a general understanding of a desirable normative framework to guide future governmental conduct affecting foreign investment. In this, as in other fields, a sound legal framework, in terms of the availability of clear, stable and reasonable general rules as well as of honest and efficient mechanisms of implementation, enforcement and dispute settlement, is essential. Obviously, such a framework, necessary as it is, cannot be expected alone to cause a major shift in the conditions of investment markets or in investor attitudes towards such markets. Establishing a sound legal and regulatory framework must therefore be seen as one of many basic requirements which together can make a difference in investment decisions and behavior. Providing conditions

of political stability, reducing macro-economic imbalances and economic uncertainties, lowering price distortions and improving the functioning of factor markets generally, strengthening financial institutions, improving physical infrastructure and government administration and ensuring the availability of trained, disciplined labor, including white collar and supervisory labor, and of relevant information, along with the presence of successfully operating foreign investors, are other essential requirements which allow an appropriate legal framework to produce the desired results, not only for the growth of foreign investment but for private sector development generally.[10] The need for international legal standards is increased by the quest for improved investment climates on a worldwide scale and the uncertainty surrounding international law rules in this field at present. As the latest UNCTC report indicated "[t]he question is no longer whether international norms should exist, but whether the international framework as it exists today is sufficient, or indeed, adequate to ensure stable, reliable and mutually beneficial foreign investment relations in the new economic and political landscape."[11]

6. While the UNCTC continues its efforts to codify internationally agreed rules to govern the future behavior of foreign investors and their host countries, this report and the proposed guidelines attached to it attempt to identify a set of principles which, it is hoped, are both acceptable in view of recent trends, and likely to enhance the prospects of investment flows to developing countries. Such recommended guidelines may thus guide further work on the subject on the national and international levels. To the extent that the practice of States conforms to these recommended guidelines in a consistent manner and reflects a general conviction of their binding character, the guidelines may then positively influence the development of customary international law in so far as they do not already reflect its rules. While the guidelines could serve these important purposes, they are clearly not intended to constitute part of World Bank loan conditionality or to assume for the Bank a legislative role which it does not have.

7. The remaining parts of this report provide explanatory notes to the proposed guidelines and are meant to facilitate their understanding and help in paving the way for their general acceptability. In reading these guidelines, it is of particular importance to bear in mind the following factors:

i) The proposed guidelines address, and are meant to apply to all member States and indeed to the world community at large; they are not addressed only to developing countries or to a specific coherent regional group of countries.

ii) The proposed guidelines address the conduct of States vis à vis foreign investors but not the conduct of foreign investors. The exclusion of the latter topic is not due to its lack of relevance or importance; it only reflects an understanding of the request made by the Development Committee and a desire to avoid repetition of the comprehensive work carried out by UNCTC, and earlier by the OECD, in this field.

iii) The proposed guidelines, being prepared for a practical purpose and not as an academic exercise, are written with a sense of realism, bearing in mind existing legal instruments, complemented by desirable practices consistent with World Bank Group policies.

iv) The proposed guidelines are meant to present a general framework which complements, but cannot substitute for the broad array of international instruments consisting of bilateral investment treaties, regional conventions and other instruments of broader application issued by specialized organizations such as the ILO, GATT, OECD, EC and others, all with the view of securing stable investment conditions in the territories of their members. In this respect, the guidelines, if adopted, would be relevant to situations where such bilateral treaties and other instruments do not exist or are silent on matters provided for in the guidelines. Thus, while the guidelines represent another step in the overall international effort to improve investment conditions and in the continuous evolution of improved standards in this area, they provide a foundation on which other instruments, especially bilateral treaties, may further build.

v) Last, but not least, the proposed guidelines are meant to serve the purpose of promotion and encouragement of foreign investments, so that such investments may increase in volume and spread out to as many countries as possible, and so that their flows may be governed only by economic considerations and not be hampered by avoidable non-commercial factors.

SCOPE OF APPLICATION OF THE PROPOSED GUIDELINES

8. Guideline I of the proposed guidelines delineates their intended scope and purpose. The guidelines may be applied by members of the World Bank Group and other States in their efforts to attract increased flows of private foreign investment. However, the guidelines would not by themselves have a binding or mandatory effect. This is made clear by the contrast that Section 1 of Guideline I draws between the guidelines and such binding instruments as pertinent bilateral and multilateral treaties. The proposed guidelines would be subject to any such treaties and should facilitate the conclusion of more bilateral investment treaties. At the same time, the guidelines may play a useful role in complementing binding instruments in the field of foreign investment. As already indicated, the guidelines incorporate lessons gained from experience of the practices and policies that may be conducive to building an attractive investment climate.

9. A particular practical contribution that the guidelines may make would, as suggested in Section 1 of Guideline I, be to assist in the development of domestic legal rules on foreign investment. For the drafters of national laws on foreign investment, the provisions of the guidelines may, depending on the circumstances, needs and policies of

the country concerned, be suggestive of desired provisions in the laws; or the guidelines may simply serve as a check-list of the types of matters that the laws might usefully address. In this context, the guidelines could also help in the coordination of technical assistance to countries in the formulation of investment laws on the basis of a minimum of broadly acceptable standards. More importantly, the guidelines may help in the progressive development of international principles and rules on foreign investment by arbitrators and scholars and may be reflected over time in the practice of States which do not already follow similar standards. The practical value of the guidelines in all these respects is enhanced by the fact that they also present general principles and current trends inferred from extensive comparative background studies of bilateral investment treaties, multilateral treaties and other instruments pertaining to foreign investment, international arbitral awards and writings of international law experts, as well as national investment codes.[12] Thus, the proposed guidelines, while not having a binding character as such, have a basis in existing legal instruments and may not be inconsistent with what some sources may consider to be settled international law. Their adoption is recommended however without prejudice to the different positions held by States and scholars on what international law may or may not require at this stage of its development.

10. The various potential contributions of the guidelines are nevertheless essentially legal in character, as envisaged in the Development Committee's request. Hence the proposed guidelines are in large measure drafted in a normative manner (while using language that is as simple and clear as possible). This would not, of course, itself impart to the guidelines any legal force. As already emphasized, the proposed guidelines are not intended to, nor could they, supersede by themselves such binding instruments as national laws or treaties. Instead, such legal force as the guidelines might eventually acquire would depend on their incorporation by States into domestic or international law in the ways described above.

11. The guidelines are meant to apply to private foreign investments. However, the broad general principles set out in the guidelines equally apply to investments made by foreign public entities such as foreign State enterprises or intergovernmental organizations. They also have obvious relevance to investments that are made by local nationals, and in that sense domestic, but with funds brought in from abroad.[13]

12. As they would be intended to assist in the encouragement of private foreign investment generally, the guidelines are purposely broad in scope. Thus while they may in several respects be particularly relevant to private foreign direct investment,[14] there is no reason to limit their application to such investment, to the exclusion of portfolio investment.

13. Indeed beyond specifying that they should be private and foreign, the proposed guidelines contain no restrictions as to the nature of the covered investments. In this respect, the guidelines would be similar to most bilateral investment treaties and multilateral instruments which either adopt broad definitions of covered investments or do not qualify them at all.[15] Thus the guidelines would apply to indirect, as well as to

direct, investments and to modern contractual and other new forms of investment where funds, equipment, technology and/or services are provided in a variety of continuously evolving ways, as long as the investor's return depends in whole or in part on the fortunes of the enterprise, as well as to traditional types of foreign investment such as equity contributions and concessions. The proposed guidelines could in general also apply to investments made in local as well as foreign currencies and to investments made in kind as well as in monetary form. They similarly contain no restrictions as to the nature of the covered foreign investors themselves, which may be corporate entities as well as individuals.[16]

14. State and nationals are other terms frequently used in the proposed guidelines. In foreign investment matters as in other fields, States generally act through their responsible agencies or other public entities. In addition, nationals of a State may include not only individuals who have the nationality of a State but also companies and similar bodies established there. To avoid any misunderstanding, Section 1 of Guideline I specifies that the guidelines are intended generally to cover the stance of a State (or any constituent subdivision or institution acting as the instrumentality or agency thereof) in respect of both individuals and juridical persons possessing the nationality of another State under the law of that State.[17]

15. The guidelines, seeking to set out a general framework for the treatment of foreign investors by their host States, cover each of the main areas in this respect, namely the admission of foreign investment, standards of treatment and transfer of capital and net revenues, expropriation and its compensation and the settlement of disputes. While, as earlier explained, rules regarding the conduct of foreign investors in their host States are not covered, the guidelines only envisage investments made and carried out in good faith and in complete compliance with local legal requirements. This fundamental assumption, which is often articulated in existing multilateral instruments on the treatment of foreign investment, is emphasized in Section 2 of Guideline I and is also reasonably reflected in Section 9 of Guideline IV.

16. Obvious differences distinguish the respective situations of foreign and local investors. Arrangements for the eventual repatriation of investment capital and returns, for example, are typically made with foreign investors only in mind. However, the situations of foreign and local investors may be similar to each other in many more respects. Experience indicates that, to the extent the circumstances of foreign and local investors are thus essentially similar, their equal treatment and hence competition on an equal footing, are important factors in creating a sound investment climate. The practice of granting foreign investors special privileges unwarranted by their particular circumstances may distort trade and competition and, in the final analysis, contribute little to the attraction of foreign investment. As is underscored by Section 3 of Guideline I, the guidelines are not intended to endorse the extension of such special privileges to foreign investors. This does not however derogate from the fact that in some respects the nature of the investment or of the investor as foreign may justify a different treatment as indicated above.

ADMISSION

17. Proposed Guideline II covers the question of the admission or entry of foreign investments into host countries. Like corresponding introductory provisions of most bilateral investment treaties and many multilateral instruments and national investment codes, Section 1 of Guideline II makes explicit the need for host countries to encourage foreign investment. In so doing, the Section calls attention to the fact that the encouragement of foreign investment may usefully be directed not only to contributions of capital but also to the transfers of the technology, knowledge and skills that frequently accompany foreign direct investment and add to its value for the efficiency and competitiveness of the host country.[18]

18. Section 2 of Guideline II gives practical expression to the general principle set forth in Section 1. In common with the provisions of many bilateral and multilateral investment treaties and national investment codes, Section 2 envisages that host countries will facilitate the admission and establishment of foreign investments. Particular reference is made in this connection to the need to avoid overregulation of and the erection of unnecessary bureaucratic obstacles to admission. In this respect, the proposed guidelines may be compared to many modern national investment codes which seek to do away in principle with admission procedures and, where such procedures are necessary, to streamline them through such devices as "one-stop shops" for investment approvals.[19]

19. Some regulations on admission exist however in all legal systems. Section 3 of Guideline II makes it clear that States maintain the right to make such regulations. In this respect, the guidelines are consistent with most bilateral and multilateral investment treaties which also recognize that the admission of foreign investment is ultimately a matter for each State to decide upon and regulate in the exercise of its sovereignty.[20]

20. However, Section 3 of Guideline II cautions against a restrictive approach and in particular against the inclusion in such regulations of certain performance requirements (such as minimum local ownership and staffing or export targets) as conditions of admission of foreign investment. As the Section explains, experience indicates that the imposition of such requirements may deter investments or encourage abuses. Reflecting this experience, performance requirements of these kinds are in fact becoming rare in national investment codes. Such codes increasingly take the approach of making admission a largely automatic process, confining exclusions or approval requirements to specified types of investment judged in need of such control.[21] Section 3 of Guideline II endorses this approach, while pointing out that the fact that a given investment requires no specific approval does not, of course, exempt it from the host State's laws and regulations which typically require registration and expect full compliance.

21. Sections 4 and 5 of Guideline II mention especially important types of exclusions that States may legitimately make under the liberal approach endorsed by Section 3. Thus States may open admission to investments without the need for prior approval but exclude from their territories foreign investments which threaten national

security under clearly defined requirements or which belong to sectors reserved by the law of the State to its nationals on account of the State's economic development objectives or national interest requirements. Beyond this, there may be other exclusions of investments that would apply equally to national and foreign investments. Such exclusions would relate to investments which are contrary to ordre public (sometimes translated into English as "public policy"), i.e. investments that violate fundamental values of society in the country concerned as defined in its laws and judicial practice, and investments that adversely affect the environment or public health. These limited types of exclusion are a standard feature of national investment codes. It is important to note, however, that exclusions of foreign investment are not meant to be applied lightly by the host State, but rather as limited exceptions after careful consideration. This point is recalled in Section 4 of Guideline II.

22. Investment codes also frequently reserve to nationals investments in sectors where it is considered that the strict exigencies of national interests demand such local control of the sectors concerned. As in some of the more recent codes, however, this latter type of restriction should be limited to sectors which are normally by nature of primarily local interest in any event. Section 4 of Guideline II recognizes that such limited restrictions may be inevitable; it does not suggest them as a rule but as an exception.

23. Assessments of local investment conditions invariably precede the decision of a serious investor actually to make an investment in a country. In order to attract foreign investments, States may find it useful actively to facilitate such assessments by prospective investors. Of special importance in this connection is the identification of relevant current local legal requirements and policies. Language and cultural differences can make this a particularly onerous undertaking for foreign investors. Their task in this respect may be partially eased by consolidating in one publication the main rules that will apply to foreign investors. Such an investment handbook may summarize the applicable rules, refer to all relevant laws and regulations and provide other information that intending investors typically require, whether or not they are reflected in an investment code.[22] Apart from the great interest of foreign investors in such a publication, it may provide a good occasion for host States also to assess the appropriateness of their foreign investment regimes. Some host States follow the approach of making available such handbooks or other summaries and Section 6 of Guideline II commends the practice.

TREATMENT

24. Guideline III of the proposed guidelines covers both the general standards of the treatment to be accorded to foreign investors by their host States and particular aspects of such treatment, notably the transfer of investment capital and returns.

25. A standard of treatment is by definition a general criterion. It clearly could lose much of its value if it only applied to parts of the activities of foreign investors. In fact, bilateral investment treaties and multilateral instruments that lay down general standards of treatment appear never to restrict the scope of the standard in this way. Accordingly, Section 1 of Guideline III makes it clear that the level of treatment recommended would cover not only the establishment of an investment but also the various aspects of its operation and the activities reasonably ancillary to it including the ultimate disposal of the investment.[23] In so doing, the Section recalls that the Guidelines are meant to apply simultaneously to all States. It also emphasizes that the detailed standards provided for in the Guidelines are subject to applicable bilateral treaties, multilateral conventions and other binding international instruments as well as to generally accepted rules of customary international law.

26. Most bilateral investment treaties and several multilateral instruments in the field prescribe an objective standard of "fair and equitable" treatment to be accorded to foreign investors. Section 2 of Guideline III follows this example and relates the standard to the guidelines as a whole.

27. Most bilateral investment treaties also require that foreign investors be accorded treatment that, in addition to being fair and equitable, is as favorable as that accorded by States to their own nationals. Many multilateral instruments and national investment codes similarly provide for a supplementary standard of national treatment. One important aspect of this standard is that foreign investors should not lack the protection and security afforded to nationals, for example with respect to the safeguarding of their persons or property interests. Another important implication of the standard is that foreign investors should not, in comparison with nationals, be put at a competitive disadvantage in respect of access to the permits or authorizations necessary to conduct business operations in the country concerned. These factors are all taken into account in Section 3(a) of Guideline III, which elaborates on the principle of "protection and security" and recommends that, in the application of this principle, foreign investors be granted treatment as favorable as that granted to nationals, provided, of course, that investors' interests and rights over their property, including intellectual property, are thereby fully protected in all its aspects of ownership, control and benefits and, more generally, that the treatment is also fair and equitable.

28. Section 3(a) of Guideline III recalls that foreigners may be thus assimilated to nationals to the extent that the circumstances of the two groups are similar. As indicated earlier, obvious differences between the situations of foreigners and nationals may call for them to be treated differently in certain areas. Section 3(b) of Guideline III recommends

that, where this is the case, the host State's rules should not discriminate among different foreign investors on the grounds of their respective nationalities. In this respect, the proposed guidelines are similar to several multilateral instruments on investment formulated in both industrial and developing country fora and provide for the equivalent of a "most favored nation clause" which is the formula typically used in the context of bilateral treaties.

29. At the same time, many bilateral investment treaties in particular allow for the drawing of distinctions in the treatment of foreign investors on the basis of membership in such treaty arrangements as customs unions and free trade areas. Section 4 of Guideline III acknowledges this common exception which, in the present context, can be viewed as another application of the principle that the proposed guidelines are subject to applicable treaties. Consistent with the approach taken under the General Agreement on Tariffs and Trade (GATT), however, investors from third countries should not as a result be accorded less favorable treatment than that which they enjoyed prior to the formation of the customs union or comparable arrangement.

30. In addition to the general standards of treatment, the proposed guidelines provide several concrete illustrations of treatment conducive to attracting foreign investment. These include the timely issuance of such authorizations as may be required for the smooth operation of investments. In this respect, the guidelines reflect the spirit of modern national investment codes the provisions of which typically seek to facilitate and expedite such authorizations.[24] Such codes sometimes still require foreign investors to recruit a minimum number of their personnel locally. However, this approach is increasingly being abandoned in favor of one emphasizing market freedom in hiring. While mentioning the normal practice of following certain procedures to establish the need for foreign personnel, Section 5(b) of Guideline III recommends a flexible approach as one more suited to stimulate foreign investment. It recognizes the importance of labor market flexibility in this and other areas, and emphasizes in particular the investor's freedom to fill top management positions regardless of nationality. Such flexibility will normally result in largely local hiring in any case because of the normally higher cost of foreign personnel.

31. The transfer of funds abroad is another fundamental aspect of the treatment of foreign investment. Such funds include the salaries and savings of expatriate personnel, investment profits, amounts needed to service debts and other contractual obligations of the investment enterprise, as well as investment liquidation or sale proceeds. Minimization of restrictions on the transfer of such funds is a hallmark of existing instruments that is reflected in the proposed guidelines. Thus many bilateral investment treaties envisage that foreign investors should be free to repatriate their net profits; like several multilateral instruments, Section 6(1) of Guideline III provides for the same freedom. Obviously, this freedom may be subject to exceptions provided for in binding international instruments such as the Articles of Agreement of the International Monetary Fund (IMF) (which prevail over these Guidelines).[25] As in the case of several bilateral investment treaties and over a dozen national investment codes, comparable freedom of transfer is envisaged

by Section 6(1) for salary and savings remittances of foreign personnel and for debt service and other contractual payments. Bilateral and multilateral investment instruments and national investment codes typically provide for similar freedom of transfer in respect of investment liquidation proceeds. In view of the large sums that such proceeds may involve, some bilateral investment treaties and national investment codes refer to the exception of effecting transfer of liquidation proceeds over limited periods defined in many treaties (of up to five years) where this is dictated by the balance of payments positions of the countries concerned. Section 6(1) of Guideline III likewise refers to this exception only in the context of the repatriation of investment liquidation or sale proceeds, as a derogation from the rule of free transfer when necessitated by the lack of adequate foreign exchange in the central bank (or similar agency) at the time the request for transfer is made and, in all cases, subject to the payment of interest. Finally, Section 6(1) of the Guideline also refers to freedom of transfer of other amounts such as those to which an investor may be entitled as compensation for expropriation or under a judicial or arbitral decision.

32. Bilateral investment treaties and several multilateral instruments contain provisions designed to assure that amounts may be transferred in currencies usable to the investor. In this connection, Section 6(2) of Guideline III, in a manner similar to bilateral investment treaties, refers to currencies imported by the investors concerned (if the currencies remain convertible), currencies designated by the IMF as freely usable, or currencies accepted by the investors. Obviously, only the latter two methods will apply to investments which do not take the form of monetary contributions. Bilateral investment treaties also specify that transfers will be made at prevailing exchange rates. In this connection, some bilateral investment treaties refer to official rates of exchange, others to exchange rates determined in accordance with IMF regulations, and some to the market rate of exchange. In the context of foreign investments, the latter rate may in general be likely to be a particularly reliable measure of the actual value of the local currency concerned. Accordingly, Section 6(2) of Guideline III, in recommending that transfers be authorized at exchange rates prevailing on the date of the transfer, refers to the market rate of exchange applicable to the transaction concerned.

33. Section 6(3) of Guideline III also recommends the payment of interest on the local currency received by the banking authorities of the host State in respect of any delays in effecting the required transfers. Such interest would, in particular, compensate the investor for delays in the transfer of the local currency amount representing liquidation proceeds in the exceptional cases when, as foreseen by Section 6(1)(d) of Guideline III, such transfer may be made by installments. Comparable provisions on interest for transfer delays may be found in some but not all bilateral investment treaties.

34. Under the applicable law, which will normally be the law of the host State, the investor might be entitled to compensation for loss due to events of international or civil strife, such as war or revolution. Section 6(4) of Guideline III recommends that the Guideline's provisions on transfer of capital should also apply to the transfer of any such compensation to which the investor may thus be entitled. In this respect, the proposed

guidelines may be compared to provisions of many bilateral investment treaties calling for such compensation to be freely transferable.

35. If the investor so chooses, it is clearly normally in the best interests of the host State that investment returns and liquidation proceeds be reinvested there rather than repatriated.[26] Section 7 of Guideline III accordingly recommends that host States permit and facilitate such reinvestment. This does not in any way imply that the State should create obstacles to free transfer.

36. After the provision of Section 8 of Guideline III on the need to prevent and control corrupt business practices (referred to in paragraph 2 above), Section 9 of this Guideline presents recommendations of "best practice" with respect to the further area of tax exemptions and other fiscal incentives. The Section cautions against the granting by host States of such exemptions and incentives, a practice which is increasingly motivated by competition among host States. It will be recalled that these exemptions or incentives often represent unjustified sacrifices on the part of host States or serve as poor substitutes for appropriate overall policies affecting investments. Foreign investors may in fact be discouraged by the instability or unpredictability of a regime that incorporates tax holidays and the like followed by significant increases in tax rates to offset the initially foregone revenues of the host State. As Section 9 of Guideline III explains, reasonable and stable tax rates provide better incentives to investors. Where the host State decides that fiscal exemptions are nevertheless justified, Section 9 of Guideline III recommends that, in keeping with other parts of the proposed guidelines, they be made available, for the types of activity to be encouraged, to foreign and national investors equally and with a minimum of bureaucratic discretion in the matter. On the other hand, Section 10 of Guideline III mentions a number of measures[27] which some investors' countries take to assist investment flows to developing countries; in this respect, the Section recognizes the granting of fiscal incentives to investors by their home States as a possibly effective means of encouraging such flows.

EXPROPRIATION AND UNILATERAL ALTERATIONS OR TERMINATION OF CONTRACTS

37. Guideline IV covers the subject of expropriation of foreign investments. The Guideline also addresses the question of unilateral changes by host governments of contracts with foreign investors for non-commercial reasons, a subject which is often associated with and made subject to several of the same principles as those governing expropriation. These have been controversial subjects. The background studies on which the proposed guidelines are partly based show that there is however significant consensus on most of the issues involved. Building on this consensus and best practice, the proposed guidelines offer practical solutions to such issues and avoid the ideological approaches that have led to much of the controversy in the past.

38. Many national investment codes, virtually all bilateral investment treaties and most pertinent multilateral instruments contain provisions to the effect that host States may expropriate foreign investments only if the takings are done in accordance with applicable legal procedures, for a public purpose and against payment of compensation. These provisions are typically broad enough to encompass partial as well as total expropriations of foreign investments. The provisions in the bilateral investment treaties and multilateral instruments also often explicitly cover not only outright expropriations but also measures, such as excessive and repetitive tax or regulatory measures, that have a de facto confiscatory effect in that their combined effect results in depriving the investor in fact from his ownership, control or substantial benefits over his enterprise, even when each such measure taken separately does not have this effect (so-called "creeping expropriations").[28] A further element that frequently appears in the bilateral investment treaties and multilateral instruments is that takings by the host State of foreign investments should not discriminate among investors on the basis of their nationalities. All of these elements are also supported by international arbitral awards and scholarly writings on the subject. Each element is incorporated into the definition of permissible expropriations in Section 1 of Guideline IV which, for the sake of clarity, adds that the required pursuit of a public purpose be in good faith.[29]

39. The point of significant disagreement over the conditions of permissible expropriations has concerned the measure of compensation for such expropriations. Most bilateral investment treaties and many western writers have adopted the well-known formula calling for "prompt, adequate and effective" compensation. Many national laws (of both industrial and developing countries) and most multilateral instruments employ more general terms to describe the required compensation, such as "just" or "appropriate." The two approaches are not, of course, mutually exclusive -- for example, compensation that is prompt, adequate and effective may also be the most appropriate. As pertinent international arbitral awards indicate, much depends in this area on the circumstances of the case at hand. With this in mind, the proposed guidelines take a practical approach to the matter, employing first the all-embracing term--appropriate--for the recommended general standard on compensation in Section 1 of Guideline IV, and then specifically applying this in Section 2 to indicate, in the context of the taking of a specific investment by a State, that compensation will normally be deemed to be appropriate if it is "adequate, effective and prompt." Sections 3-6 of Guideline IV elaborate upon this recommendation by providing important practical details suggested by judicial and arbitral experience. Of particular value in this connection are the findings of international arbitral awards which provide details on the often vague general standards embodied in treaties, other international instruments and national legislation.

40. Thus in line with many such awards--as well as significant numbers of bilateral investment treaties and multilateral instruments and some national investment codes--Section 3 of Guideline IV explains that the level of compensation for such a taking will be deemed to be "adequate" if it is based on the fair market value of the taken asset immediately before the taking occurred or the State's decision to take the asset became publicly known. Section 4 of the Guideline encourages agreements between States and

foreign investors on how this value should be determined. Where the parties fail to reach such agreement, Section 5 of Guideline IV, again following international arbitral precedent, recommends that the fair market value may be assessed by determining the price that a willing buyer would normally pay to a willing seller of the investment, after taking into account all relevant circumstances such as the nature and duration of the investment. Throughout, reasonable criteria would be applied with a view to ascertaining the market value of the investment.

41. While the guidelines would not and could hardly seek to impose rigid criteria or hard and fast rules in this respect, Section 6 of Guideline IV presents, on the basis of experience in international arbitrations in particular, different methods of valuation for different types of assets as examples of appropriate ways of determining the market worth of an investment.[30]

42. For a going concern, i.e. an enterprise consisting of income-producing assets and already in existence for a sufficient period of time to generate the data necessary for proving its profitability and the calculation, with reasonable certainty, of its income in future years (on the assumption that the taking did not take place), Section 6 of Guideline IV suggests that discounted cash flow may represent an acceptable method of valuation. This method values an income-producing asset by estimating the net cash flow which the asset would be realistically expected to generate over the course of its life, and then discounting that net cash flow by a factor that reflects the time value of money, expected inflation and the risk associated with the cash flow. This method is regarded as appropriate for valuing enterprises with a firmly established income-producing capacity because it recognizes that the economic value of such an enterprise to its owner is a function of the cash that the enterprise can be expected to produce in future. However, particular caution should be observed in applying this method as experience shows that investors tend to greatly exaggerate their claims of compensation for lost future profits.[31] Compensation under this method is not appropriate for speculative or indeterminate damage,[32] or for alleged profits which cannot legitimately accrue under the laws and regulations of the host country.[33]

43. For an enterprise lacking profitability, Section 6 of Guideline IV provides as an example of an appropriate valuation method one which looks to the assets' liquidation value. This method values an enterprise with demonstrated lack of profitability as the sum of the amounts at which the individual assets comprising the enterprise could be sold less any liabilities that the enterprise might have to meet.

44. For other assets, recourse may be had to the replacement value method. This method measures value on the basis of the amount of cash that would have been required to purchase the individual assets that have been expropriated at their actual state as of the date of the taking. This method obviously assumes that the assets in question are replaceable, which may not always be the case. In addition, the replacement value may not always reflect the value that individual assets may have had together in an enterprise. This problem may be addressed by using the book value method. Book value means the

difference between a company's assets and liabilities as recorded in its financial statements, or the amount at which the expropriated asset appears on the enterprise's balance sheet after deducting accumulated depreciation in accordance with generally accepted accounting principles. In the proposed guidelines, this method of valuation is only recommended for cases where such book value has been recently assessed and can therefore be deemed to be a fair substitute for the replacement value. In any case, the "book value" cannot present a fair methodology if it bears no relationship to the market value.

45. Sections 7 and 8 of Guideline IV consider the two other elements of the general recommendation on appropriate compensation for takings of specific investments, namely the effectiveness and timeliness of such compensation. In both respects, the Sections logically recall the proposed guidelines' recommendations on transfer of capital. It is in this context worth noting that some national investment codes and several bilateral investment treaties explicitly link their provisions on compensation for expropriation with those on transfer. In a manner similar to the transfer provision of Section 6(2) of Guideline III, Section 7 of Guideline IV thus deems compensation to be effective if it is paid in the currency originally imported by the investor (if it remains convertible at the time of transfer), in another currency designated as freely usable by the IMF or in any other currency accepted by the investor, with only the latter two methods applying to investments which do not take the form of monetary contributions.

46. As indicated earlier, many bilateral investment treaties require that compensation for expropriation be paid promptly or without delay. Of course, such treaties are only binding on the States parties to them. Countries not parties to such treaties do not always accept that prompt payment is legally required. Significant numbers of other bilateral treaties and multilateral instruments recognize that there may be reasonable delays in effecting compensation. They accordingly rule out only undue delays in payment. Elaborating on this, several treaties acknowledge that host countries may face foreign exchange stringencies and therefore allow payment of compensation by installments, subject to the payment of proper interest in respect of the deferred payments. Such circumstances and possibilities are acknowledged within narrow time limits by Section 8 of Guideline IV only as exceptions from the general rule of prompt payment in the cases justifying them. The Section refers in this context to cases where there are arrangements for the use of IMF resources or similar objective circumstances of established foreign exchange stringencies. This elaboration is well justified as Section 8 of Guideline IV, in dealing with compensation for an expropriation, addresses consequences of a deliberate decision by the State.[34] Under both Guidelines III and IV, however, the exceptions should be read as a realistic recognition of inevitable compelling circumstances, not as a permit to avoid transfers where these are possible.

47. The above general principles, which envisage ordinary takings of specific investments, may not be fully applicable in respect of certain other types of takings. For example, a foreign investor may be entitled to lesser compensation or to none at all in respect of an expropriation that results from a breach by the investor of the laws of the

host State, as may occur when the investment is used as a conduit for drug trafficking or for other criminal activity, or involves gross violations of anti-trust or environmental laws. This point is made in Section 9 of Guideline IV which of course only envisages cases of sanctions properly imposed by courts of law and assumes a proper application of the principle of proportionality (under which a minor offense, for example, should not provide a basis for such a drastic response as a taking). In this context, the Section raises the possibility of any further claims by the investor for compensation being referred to the mechanisms of settlement of disputes mentioned in Guideline V.

48. Also clearly to be distinguished from takings of specific investments are comprehensive non-discriminatory nationalizations of the kinds that take place in the context of large scale social reforms following the most exceptional circumstances of revolutionary changes, war, and similar exigencies. Many international law writers acknowledge that in such contexts States may be required to pay only partial compensation.[35] Expropriations of these kinds may typically have important international as well as domestic policy dimensions. In view of this, compensation arrangements in such unusual circumstances have in practice often been negotiated between the home and host States of the investors, resulting as a practical matter in partial compensation.[36] Without necessarily suggesting any particular outcome in these circumstances, Section 10 of Guideline IV recommends that compensation for such expropriations may more appropriately be determined through negotiations between the States involved or, failing such negotiations, by their submission of the matter to international arbitration. This provision addresses circumstances which rarely occur and which may be expected to become more uncommon in future.

49. Under the laws of most countries, State parties to commercial contracts with foreign nationals are generally bound by such contracts to the same extent as non-State parties would be. However, under many legal systems a State may in the exercise of its sovereign powers, that is, when it acts as a sovereign, not simply as a contracting party, unilaterally change, terminate or repudiate the contract. This practice is tolerated in the practice of States when done in the bona fide pursuit of a public purpose, rather than for commercial reasons, and against just compensation. Section 11 of Guideline IV recommends that such practice be subject to the same conditions of expropriation and that in such cases foreign investors should be compensated according to principles similar to those set out in the proposed guidelines for expropriation of specific investments. In this respect, the proposed guidelines reflect the findings of several international arbitral awards and international law writers.

SETTLEMENT OF DISPUTES

50. Particularly in the context of arrangements with States, disputes are normally resolved through negotiations and relatively rarely by recourse to contentious procedures. Section 1 of Guideline V further encourages the negotiated resolution of conflicts between foreign investors and their host States. In case negotiations fail, the courts of the host

State will normally and unless otherwise provided have jurisdiction over disputes arising out of investments made in the country. In most countries, it is however possible for States and foreign investors to refer their differences to such alternative mechanisms as conciliation or binding arbitration. Recourse to such mechanisms is dependent on agreement between the parties to make use of the mechanism for the dispute in question. In the field of foreign investment, parties frequently do agree to refer their disputes to arbitration in particular. This practice is endorsed by Section 1 of Guideline V.

51. One of the advantages of arbitration is that it offers parties great scope to structure as they see fit their dispute settlement procedures. Their decisions on such procedures will be embodied in their agreement to have recourse to arbitration. In this context, States in particular may, as a condition of their agreement to refer disputes with foreign investors to arbitration, require the investor to resort to local administrative or judicial remedies before initiating such arbitration. This possibility is recognized by such instruments as the Convention establishing the International Centre for Settlement of Investment Disputes (ICSID) and several bilateral investment treaties. It is not however mentioned in the Guidelines as it is rarely pursued in practice.

52. The arbitration that Guideline V envisages as a possible alternative to adjudication before national courts is indeed impartial or independent arbitration. It is widely acknowledged that in the field of international investment arbitration in particular arbitrators should be, and be seen to be, impartial and independent.[37] At the same time, arbitrators are generally chosen through appointments by the parties to the dispute in question. One of the perceived advantages of arbitration is in fact the opportunity that it thus gives parties to have their dispute decided by judges of their own choosing. In appointing arbitrators, each party may naturally wish to select persons who may be expected to be sympathetic to the point of view of the appointing party. To ensure the necessary impartiality of the tribunal as a whole, arbitral tribunals thus commonly consist of one arbitrator appointed by each side and a presiding arbitrator appointed by agreement of the parties or by a neutral appointing authority designated by the parties. An alternative that avoids the costs to the parties of a three-arbitrator panel is to submit the dispute to a sole arbitrator appointed by both parties or by a third party entrusted by them with the role of making such an appointment. Where however the appointment of a sole arbitrator or of a majority of arbitrators is made by one party only, the independence of the tribunal could easily be put in doubt. Section 2 of Guideline V emphasizes the importance of avoiding such a procedure and excludes a tribunal so constituted from the definition of independent arbitration.

53. The independence and impartiality of arbitrators receive particular emphasis in the rules of ICSID, the international conciliation and arbitration forum sponsored by the World Bank and specially designed to handle disputes between States and foreign investors.[38] Provisions for the resolution of such disputes in bilateral investment treaties, national investment codes and individual investment agreements frequently refer to the arbitration procedures of ICSID. The widespread acceptability of ICSID procedures, indicated by the large number of countries (120) that have so far signed the ICSID

Convention, and by the reference to ICSID arbitration in hundreds of large investment contracts, may be due, in addition to its relatively low cost, to the fact that it is the only form of arbitration where awards are not subject to subsequent judicial review in ICSID member countries. ICSID in fact provides two kinds of independent arbitration procedures: ICSID Convention arbitration procedures, which are available for cases where both the home and the host State of the investor are parties to the ICSID Convention; and arbitration procedures under the so-called ICSID Additional Facility, which are available for cases where either the home or the host State is not a party to the Convention. References to both types of procedures are frequently included in the provisions referred to above of bilateral investment treaties and national investment codes. Section 3 of Guideline V further encourages such use, as appropriate, of procedures provided by the ICSID Convention or Additional Facility.

NOTES

1. Report by the President of the Forty-sixth Session of the General Assembly, July 23, 1992.

2. UNCTC, The International Framework for Transnational Corporations-Report of the Secretary-General, E/C 10/1992/8, Jan. 13, 1992, para. 24 (hereinafter UNCTC Report). In addition, in 1976 the members of OECD adopted Guidelines for Multinational Enterprises which laid down standards for the activities of such enterprises. See Annex to Declaration of June 21, 1976 by Governments of OECD Member Countries on International Investment and Multinational Enterprises, in OECD, The OECD Declaration and Decisions on International Investment and Multinational Enterprises: Basic Texts 9 (1992).

3. See Section 2 of Guideline I of the proposed guidelines attached to this report. As indicated in the commentary on that section (at infra para. 15), this principle is often reflected in existing multilateral instruments on the treatment of foreign investment, such as the Lomé IV Convention and the draft UNCTC Code of Conduct on Transnational Corporations.

4. Section 4(ii) of Guideline II.

5. Section 8 of Guideline III.

6. IBRD Debt and International Finance Division, Financial Flows to Developing Countries: Current Developments, March 1992 at 9.

7. IFC, Trends in Private Investment in Developing Countries, 1992 Edition at 2 (by Guy P. Pfeffermann and Andrea Madarassy)

8. See IBRD, Global Economic Prospects and the Developing Countries 38-39 and table 3.5 (1991).

9. International Arrangements and Agreements Relating to Transnational Corporations: International Framework for Transnational Corporations, Report of the Secretary General, U.N. Doc. E/C.10/1992/8 at 5 (Feb. 18, 1992).

10. See Shihata, Factors Influencing the Flow of Foreign Investment and the Relevance of a Multilateral Guarantee Scheme, 21/3 The International Lawyer 671 (1987); MIGA and Foreign Investment (1988); and Promotion of Foreign Direct Investment--A General Account, with Particular Reference to the Role of the World Bank Group, 6 ICSID Review-Foreign Investment Law Journal 484 (1991). See also IFC, supra note 4, at 5-6; Mody & Srinavasan, Trends and Determinants of Foreign Direct Investment: An Empirical Analysis of U.S. Investment Abroad (World Bank Working Paper, Dec. 1991).

11. UNCTC Report, supra note 2, at para. 34.

12. These studies are reprinted in World Bank Group, Legal Framework for the Treatment of Foreign Investment, Vol. 1. They are the bases for the generalizations in the present report about bilateral investment treaties, multilateral instruments, national investment codes, and international arbitral awards and scholarly writings.

13. Compare Article 13(c) of the MIGA Convention which opens the possibility of assimilating local nationals to foreign investors eligible for the Agency's guarantee where the local nationals are investors transferring to the host country assets from abroad.

14. Paragraph 408 of the IMF Balance of Payments Manual (4th ed. 1977) defines direct investment as "investment that is made to acquire a lasting interest in an enterprise operating in an economy other than that of the investor, the investor's purpose being to have an effective voice in the management of the enterprise."

15. For example, many bilateral investment treaties define covered investments as including "every kind of asset." Under the MIGA Convention (art. 12), investments eligible for the Agency's guarantee potentially include virtually any "medium- or long-term form of investment." In the ICSID Convention (art. 25(i)), which like the proposed guidelines takes the broadest approach, the term "investment" is purposely undefined.

16. In potentially accommodating these various forms of investment and investors, the proposed guidelines may be compared to the MIGA Convention (at arts. 12 and 13) and MIGA's Operational Regulations (at paras. 1.01-1.19).

17. Similarly, under the ICSID Convention (art. 25), States parties may include agencies and subdivisions of States, and nationals of States may include juridical as well as natural persons from States. (Under general international law, a dual national who has the nationalities of the host State and another State or States is considered a national of the host State unless it otherwise agrees to treat him differently.)

18. See Shihata, Factors Influencing the Flow of Foreign Investment and the Relevance of a Multilateral Guarantee Scheme, supra note 10.

19. See, e.g., Mahmassani, The Legal Framework for Investment in Poland, 3 ICSID Review-Foreign Investment Law Journal 286, 297 (1988).

20. In their investment laws also, States uniformly reserve to themselves the ultimate decision on the admission of foreign investments.

21. See, e.g., Pogany, Recent Developments Relating to Foreign Investment in Hungary, 6 ICSID Review-Foreign Investment Law Journal 114 (1991).

22. Compare Wälde, Investment Policies and Investment Promotion in the Mineral Industries, 6 ICSID Review-Foreign Investment Law Journal 94, 112 (1991).

23. It can in this connection be noted that the scope of some bilateral investment treaties is explicitly extended to cover activities associated with investments as well as investments themselves.

24. See text accompanying supra note 19.

25. The latter exceptions include exchange restrictions in effect when a country became a member of the IMF and maintained as transitional arrangements and restrictions approved by the IMF. For details, see Silard, Exchange Controls and External Indebtedness; Are the Bretton Woods Concepts Still Workable?--A Perspective from the International Monetary Fund, 7 Houston Journal of International Law 53 (1984).

26. Reinvestment of investment amounts is encouraged by, inter alia, the MIGA Convention (art. 12(c)(ii)) to avoid negative effects on the balance of payments of the host country.

27. See also the paper on Resource Flows to Developing Countries prepared by World Bank and IMF staff for submission to the Development Committee in September 1992.

28. See, e.g., Dolzer, Indirect Expropriation of Alien Property, 1 ICSID Review-Foreign Investment Law Journal 41 (1986).

29. A similar precision regarding good faith is included in a provision (para. 1.36) of MIGA's Operational Regulations on the expropriation risk.

30. On the experience in international arbitrations in this respect, see, e.g., Friedland and Wong, Measuring Damages for the Deprivation of Income-Producing Assets: ICSID Case Studies, 6 ICSID Review-Foreign Investment Law Journal 400 (1991).

31. See fourth study in Legal Framework for the Treatment of Foreign Investment, Vol. I, supra note 10, at 146. See also Westberg, International Transactions and Claims Involving Government Parties--Case Law of the Iran-U.S. Claims Tribunals 252 (1991); Amerasinghe, Issues of Compensation for the Taking of Alien Property in the Light of Recent Cases and Practice, 4 International and Comparative Law Quarterly 22 (1992).

32. See Chorzow Factory Case, PCIJ Ser. A, No. 17, 1928, at 51; Amoco International Finance Corporation v. Iran, 15 Iran-U.S. C.T.R., at 238.

33. See A. de Laubadère, 2 Traité de Contrats Administratifs 556 and 1327 (1984). The same principle has been reflected in a recent ICSID award.

34. Compare supra paras. 31 and 33.

35. See, e.g., American Law Institute, Restatement (Third) of Foreign Relations Law § 712 cmt. (1987) (suggesting that "[i]n exceptional circumstances, some deviation from the standard of [full] compensation" might be justified, and mentioning in this context takings of alien property "during war or similar exigency"); 1 Oppenheim, International Law 352 (8th ed. Lauterpacht 1955) (suggesting that, "in cases in which fundamental changes in the political system and economic structure of the State or far-reaching social reforms entail interference, on a large scale, with private property..., [i]t is probable that, consistently with legal principle, [the] solution must be sought in the granting of partial compensation"). See also other writers cited in Legal Framework for the Treatment of Foreign Investment, Vol. I, supra note 12, at 142.

36. See, e.g., Lillich, Lump Sum Agreements, 8 Encyclopedia of Public International Law 367 (1985) (referring to "the nearly 200 lump sum agreements" that home and host States have negotiated since the Second World War, under which host States have, in settlement of claims occasioned by war, nationalization programs, revolutions, etc., paid fixed amounts to home States for distribution among claimants).

37. See, e.g., Redfern and Hunter, Law and Practice of International Commercial Arbitration 213-25 (2d. ed. 1991).

38. See ICSID Convention at arts. 14(1) and 40(2); Shihata, The Experience of ICSID in the Selection of Arbitrators, 6 News from ICSID, No. 1, at 4 (1989). For general descriptions of ICSID and ICSID arbitration, see, e.g., Broches, Arbitration Under the ICSID Convention (ICSID publication, 1991); Shihata, Towards a Greater Depoliticization of Investment Disputes: The Roles of ICSID and MIGA (ICSID publication, 1992); and Paulsson, ICSID's Achievements and Prospects, 6 ICSID Review-Foreign Investment Law Journal 380 (1991).

Guidelines on the Treatment of Foreign Direct Investment

The Development Committee

Recognizing

that a greater flow of foreign direct investment brings substantial benefits to bear on the world economy and on the economies of developing countries in particular, in terms of improving the long term efficiency of the host country through greater competition, transfer of capital, technology and managerial skills and enhancement of market access and in terms of the expansion of international trade;

that the promotion of private foreign investment is a common purpose of the International Bank for Reconstruction and Development, the International Finance Corporation and the Multilateral Investment Guarantee Agency;

that these institutions have pursued this common objective through their operations, advisory services and research;

that at the request of the Development Committee, a working group established by the President of these institutions and consisting of their respective General Counsel has, after reviewing existing legal instruments and literature, as well as best available practice identified by these institutions, prepared a set of guidelines representing a desirable overall framework which embodies essential principles meant to promote foreign direct investment in the common interest of all members;

that these guidelines, which have benefitted from a process of broad consultation inside and outside these institutions, constitute a further step in the evolutionary process where several international efforts aim to establish a favorable investment environment free from non-commercial risks in all countries, and thereby foster the confidence of international investors; and

that these guidelines are not ultimate standards but an important step in the evolution of generally acceptable international standards which complement, but do not substitute for, bilateral investment treaties,

therefore calls the attention of member countries to the following Guidelines as useful parameters in the admission and treatment of private foreign investment in their territories, without prejudice to the binding rules of international law at this stage of its development.

I
Scope of Application

1. These Guidelines may be applied by members of the World Bank Group institutions to private foreign investment in their respective territories, as a complement to applicable bilateral and multilateral treaties and other international instruments, to the extent that

these Guidelines do not conflict with such treaties and binding instruments, and as a possible source on which national legislation governing the treatment of private foreign investment may draw. Reference to the "State" in these Guidelines, unless the context otherwise indicates, includes the State or any constituent subdivision, agency or instrumentality of the State and reference to "nationals" includes natural and juridical persons who enjoy the nationality of the State.

2. The application of these Guidelines extends to existing and new investments established and operating at all times as bona fide private foreign investments, in full conformity with the laws and regulations of the host State.

3. These Guidelines are based on the general premise that equal treatment of investors in similar circumstances and free competition among them are prerequisites of a positive investment environment. Nothing in these Guidelines therefore suggests that foreign investors should receive a privileged treatment denied to national investors in similar circumstances.

II
Admission

1. Each State will encourage nationals of other States to invest capital, technology and managerial skill in its territory and, to that end, is expected to admit such investments in accordance with the following provisions.

2. In furtherance of the foregoing principle, each State will:
   - (a) facilitate the admission and establishment of investments by nationals of other States, and
   - (b) avoid making unduly cumbersome or complicated procedural regulations for, or imposing unnecessary conditions on, the admission of such investments.

3. Each State maintains the right to make regulations to govern the admission of private foreign investments. In the formulation and application of such regulations, States will note that experience suggests that certain performance requirements introduced as conditions of admission are often counterproductive and that open admission, possibly subject to a restricted list of investments (which are either prohibited or require screening and licensing), is a more effective approach. Such performance requirements often discourage foreign investors from initiating investment in the State concerned or encourage evasion and corruption. Under the restricted list approach, investments in non-listed activities, which proceed without approval, remain subject to the laws and regulations applicable to investments in the State concerned.

4. Without prejudice to the general approach of free admission recommended in Section 3 above, a State may, as an exception, refuse admission to a proposed investment:
   - (i) which is, in the considered opinion of the State, inconsistent with clearly defined requirements of national security; or
   - (ii) which belongs to sectors reserved by the law of the State to its nationals on account of the State's economic development objectives or the strict exigencies of its national interest.

5. Restrictions applicable to national investment on account of public policy (ordre public), public health and the protection of the environment will equally apply to foreign investment.

6. Each State is encouraged to publish, in the form of a handbook or other medium easily accessible to other States and their investors, adequate and regularly updated information about their legislation, regulations and procedures relevant to foreign investment and other information relating to their investment policies including, inter alia, an indication of any classes of investment which it regards as falling under Sections 4 and 5 of this Guideline.

III
Treatment

1. For the promotion of international economic cooperation through the medium of private foreign investment, the establishment, operation, management, control, and exercise of rights in such an investment, as well as such other associated activities necessary therefor or incidental thereto, will be consistent with the following standards which are meant to apply simultaneously to all States without prejudice to the provisions of applicable international instruments, and to firmly established rules of customary international law.

2. Each State will extend to investments established in its territory by nationals of any other State fair and equitable treatment according to the standards recommended in these Guidelines.

3. (a) With respect to the protection and security of their person, property rights and interests, and to the granting of permits, import and export licenses and the authorization to employ, and the issuance of the necessary entry and stay visas to their foreign personnel, and other legal matters relevant to the treatment of the investment as described in Section 2 above, such treatment will, subject to the requirement of fair and equitable treatment mentioned above, be as favorable as that accorded by the State to national investors in similar circumstances. In all cases, full protection and security will be accorded to the investor's rights regarding ownership, control and substantial benefits over his property, including intellectual property.

(b) As concerns such other matters as are not relevant to national investors, treatment under the State's legislation and regulations will not discriminate among foreign investors on grounds of nationality.

4. Nothing in this Guideline will automatically entitle nationals of other States to the more favorable standards of treatment accorded to the nationals of certain States under any customs union or free trade area agreement.

5. Without restricting the generality of the foregoing, each State will:

(a) promptly issue such licenses and permits and grant such concessions as may be necessary for the uninterrupted operation of the admitted investment; and

(b) to the extent necessary for the efficient operation of the investment, authorize the employment of foreign personnel. While a State may require the foreign investor to reasonably establish his inability to recruit the required personnel locally, e.g., through local advertisement, before he resorts to the recruitment of foreign personnel, labor market flexibility in this and other areas is recognized as an important element in a positive investment environment.

Of particular importance in this respect is the investor's freedom to employ top managers regardless of their nationality.

6. (1) Each State will, with respect to private investment in its territory by nationals of the other States:

(a) freely allow regular periodic transfer of a reasonable part of the salaries and wages of foreign personnel; and, on liquidation of the investment or earlier termination of the employment, allow immediate transfer of all savings from such salaries and wages;

(b) freely allow transfer of the net revenues realized from the investment;

(c) allow the transfer of such sums as may be necessary for the payment of debts contracted, or the discharge of other contractual obligations incurred in connection with the investment as they fall due;

(d) on liquidation or sale of the investment (whether covering the investment as a whole or a part thereof), allow the repatriation and transfer of the net proceeds of such liquidation or sale and all accretions thereto all at once; in the exceptional cases where the State faces foreign exchange stringencies, such transfer may as an exception be made in installments within a period which will be as short as possible and will not in any case exceed five years from the date of liquidation or sale, subject to interest as provided for in Section 6 (3) of this Guideline; and

(e) allow the transfer of any other amounts to which the investor is entitled such as those which become due under the conditions provided for in Guidelines IV and V.

(2) Such transfer as provided for in Section 6 (1) of this Guideline will be made (a) in the currency brought in by the investor where it remains convertible, in another currency designated as freely usable currency by the International Monetary Fund or in any other currency accepted by the investor, and (b) at the applicable market rate of exchange at the time of the transfer.

(3) In the case of transfers under Section 6 (1) of this Guideline, and without prejudice to Sections 7 and 8 of Guideline IV where they apply, any delay in effecting the transfers to be made through the central bank (or another authorized public authority) of the host State will be subject to interest at the normal rate applicable to the local currency involved in respect of any period intervening between the date on which such local currency has been provided to the central bank (or the other authorized public authority) for transfer and the date on which the transfer is actually effected.

(4) The provisions set forth in this Guideline with regard to the transfer of capital will also apply to the transfer of any compensation for loss due to war, armed conflict, revolution or insurrection to the extent that such compensation may be due to the investor under applicable law.

7. Each State will permit and facilitate the reinvestment in its territory of the profits realized from existing investments and the proceeds of sale or liquidation of such investments.

8. Each State will take appropriate measures for the prevention and control of corrupt business practices and the promotion of accountability and transparency in its dealings with

foreign investors, and will cooperate with other States in developing international procedures and mechanisms to ensure the same.

9. Nothing in this Guideline suggests that a State should provide foreign investors with tax exemptions or other fiscal incentives. Where such incentives are deemed to be justified by the State, they may to the extent possible be automatically granted, directly linked to the type of activity to be encouraged and equally extended to national investors in similar circumstances. Competition among States in providing such incentives, especially tax exemptions, is not recommended. Reasonable and stable tax rates are deemed to provide a better incentive than exemptions followed by uncertain or excessive rates.

10. Developed and capital surplus States will not obstruct flows of investment from their territories to developing States and are encouraged to adopt appropriate measures to facilitate such flows, including taxation agreements, investment guarantees, technical assistance and the provision of information. Fiscal incentives provided by some investors' governments for the purpose of encouraging investment in developing States are recognized in particular as a possibly effective element in promoting such investment.

IV
Expropriation and Unilateral Alterations or Termination of Contracts

1. A State may not expropriate or otherwise take in whole or in part a foreign private investment in its territory, or take measures which have similar effects, except where this is done in accordance with applicable legal procedures, in pursuance in good faith of a public purpose, without discrimination on the basis of nationality and against the payment of appropriate compensation.

2. Compensation for a specific investment taken by the State will, according to the details provided below, be deemed "appropriate" if it is adequate, effective and prompt.

3. Compensation will be deemed "adequate" if it is based on the fair market value of the taken asset as such value is determined immediately before the time at which the taking occurred or the decision to take the asset became publicly known.

4. Determination of the "fair market value" will be acceptable if conducted according to a method agreed by the State and the foreign investor (hereinafter referred to as the parties) or by a tribunal or another body designated by the parties.

5. In the absence of a determination agreed by, or based on the agreement of, the parties, the fair market value will be acceptable if determined by the State according to reasonable criteria related to the market value of the investment, i.e. in an amount that a willing buyer would normally pay to a willing seller after taking into account the nature of the investment, the circumstances in which it would operate in the future and its specific characteristics, including the period in which it has been in existence, the proportion of tangible assets in the total investment and other relevant factors pertinent to the specific circumstances of each case.

6. Without implying the exclusive validity of a single standard for the fairness by which compensation is to be determined and as an illustration of the reasonable determination by

a State of the market value of the investment under Section (5) above, such determination will be deemed reasonable if conducted as follows:

(i) for a going concern with a proven record of profitability, on the basis of the discounted cash flow value;

(ii) for an enterprise which, not being a proven going concern, demonstrates lack of profitability, on the basis of the liquidation value;

(iii) for other assets, on the basis of (a) the replacement value or (b) the book value in case such value has been recently assessed or has been determined as of the date of the taking and can therefore be deemed to represent a reasonable replacement value.

For the purpose of this provision:

- a "going concern" means an enterprise consisting of income-producing assets which has been in operation for a sufficient period of time to generate the data required for the calculation of future income and which could have been expected with reasonable certainty, if the taking had not occurred, to continue producing legitimate income over the course of its economic life in the general circumstances following the taking by the State;
- "discounted cash flow value" means the cash receipts realistically expected on the enterprise in each future year of its economic life as reasonably projected minus that year's expected cash expenditure, after discounting this net cash flow for each year by a factor which reflects the time value of money, expected inflation, and the risk associated with such cash flow under realistic circumstances. Such discount rate may be measured by examining the rate of return available in the same market on alternative investments of comparable risk on the basis of their present value;
- "liquidation value" means the amounts at which individual assets comprising the enterprise or the entire assets of the enterprise could be sold under conditions of liquidation to a willing buyer less any liabilities which the enterprise has to meet;
- "replacement value" means the cash amount required to replace the individual assets of the enterprise in their actual state as of the date of the taking; and
- "book value" means the difference between the enterprise's assets and liabilities as recorded on its financial statements or the amount at which the taken tangible assets appear on the balance sheet of the enterprise, representing their cost after deducting accumulated depreciation in accordance with generally accepted accounting principles.

7. Compensation will be deemed "effective" if it is paid in the currency brought in by the investor where it remains convertible, in another currency designated as freely usable by the International Monetary Fund or in any other currency accepted by the investor.

8. Compensation will be deemed to be "prompt" in normal circumstances if paid without delay. In cases where the State faces exceptional circumstances, as reflected in an arrangement for the use of the resources of the International Monetary Fund or under similar objective circumstances of established foreign exchange stringencies, compensation in the currency designated under Section 7 above may be paid in installments within a period which will be as short as possible and which will not in any case exceed five years

from the time of the taking, provided that reasonable, market-related interest applies to the deferred payments in the same currency.

9. Compensation according to the above criteria will not be due, or will be reduced in case the investment is taken by the State as a sanction against an investor who has violated the State's law and regulations which have been in force prior to the taking, as such violation is determined by a court of law. Further disputes regarding claims for compensation in such a case will be settled in accordance with the provisions of Article V of these Guidelines.

10. In case of comprehensive non-discriminatory nationalizations effected in the process of large scale social reforms under exceptional circumstances of revolution, war and similar exigencies, the compensation may be determined through negotiations between the host State and the investors' home State and failing this, through international arbitration.

11. The provisions of Section 1 of this Guideline will apply with respect to the conditions under which a State may unilaterally terminate, amend or otherwise disclaim liability under a contract with a foreign private investor for other than commercial reasons, i.e., where the State acts as a sovereign and not as a contracting party. Compensation due to the investor in such cases will be determined in the light of the provisions of Sections 2 to 9 of this Guideline. Liability for repudiation of contract for commercial reasons, i.e., where the State acts as a contracting party, will be determined under the applicable law of the contract.

V
Settlement of Disputes

1. Disputes between private foreign investors and the host State will normally be settled through negotiations between them and failing this, through national courts or through other agreed mechanisms including conciliation and binding independent arbitration.

2. Independent arbitration for the purpose of this Guideline will include any ad hoc or institutional arbitration agreed upon in writing by the State and the investor or between the State and the investor's home State where the majority of the arbitrators are not solely appointed by one party to the dispute.

3. In case of agreement on independent arbitration, each State is encouraged to accept the settlement of such disputes through arbitration under the Convention establishing the International Centre for Settlement of Investment Disputes (ICSID) if it is a party to the ICSID Convention or through the "ICSID Additional Facility" if it is not a party to the ICSID Convention.

PROGRESS REPORT ON TRADE POLICY DEVELOPMENTS

(Prepared jointly by the staffs of the
International Monetary Fund and the World Bank)

I. INTRODUCTION

1. At its Spring 1992 meeting, the Development Committee reviewed in some detail the interlinkages between the policies of the industrial and developing countries, emphasizing trade aspects. This paper updates trade policy developments and the status (at the time of writing) of the Uruguay Round. Last spring's background paper for the Development Committee on trade aspects featured the role of the Fund and the Bank in furthering trade liberalization among their members through financial and technical assistance and policy advice. This report describes collaboration of the Bretton Woods institutions with the GATT and illustrates the GATT's surveillance role under its new Trade Policy Review Mechanism in an annex highlighting key elements of the reviews of industrial countries.

II. TRADE POLICY DEVELOPMENTS

2. Recent trade policy developments in industrial countries continue to be characterized by reliance on unilateral and bilateral approaches to ensure maintenance or expansion of market shares and an increasing trend toward regionalism. This has occurred against the background of a difficult economic environment and considerable uncertainty on the outcome of the Uruguay Round of multilateral trade negotiations geared to improving market access and strengthening multilateral disciplines. As trade tensions remain high, trade disputes proliferate, and many are still handled at the bilateral level. However, recourse to GATT's dispute settlement mechanism has risen. While the incidence of adoption of GATT panel recommendations has increased since the streamlining of procedures, the record on implementation of panel recommendations remains disappointing. In more than two-thirds of the panel reports adopted since the Uruguay Round began, implementation has been absent or inadequate. Many of the cases of trade friction are among industrial countries themselves (for example, the United States - European Community (EC) dispute over EC oilseeds subsidies, which has been dealt with multilaterally under the GATT, has resulted in the threat of sanctions and counter-sanctions). Some cases involve developing countries (for example, in April 1992, the United States named India, Thailand and Taiwan, China for investigations under its Special 301 provisions on intellectual property rights). Other cases of trade friction involve both industrial and developing countries (for example, attempts to negotiate disciplines under the proposed Multilateral Steel Arrangement were suspended in March 1992 and the U.S. steel industry has filed wide-ranging petitions recently against allegedly dumped/subsidized imports from many countries, including Brazil, France, Germany, Japan, Korea, and Mexico). Areas of export interest to developing countries--such as textiles and clothing, footwear, agriculture, petrochemicals, and electronics--continue to be subject to significant nontariff barriers in industrial country markets, including special arrangements outside the multilateral system.

3. In general, industrial countries have held back on unilateral liberalization in the expectation of implementing multilaterally negotiated liberalization under the Uruguay Round, now in its sixth year. There are some noteworthy exceptions such as Australia, New Zealand, and Sweden--the latter, for example, eliminated all quantitative import restrictions on textiles, clothing and footwear in 1991-92.

The Multi-Fibre Arrangement (MFA) regulating trade in textiles and clothing was extended to end-December 1992 in the expectation that a Uruguay Round agreement would come into force by 1993. Reliance on protection/subsidies in agriculture remains high--a recent OECD study estimated production subsidy equivalents (in percent of producer prices) in 1991 as 66 percent for Japan, 49 percent for the EC, and 30 percent for the United States. A positive development was the EC agreement in June 1992 on a significant reform of the Common Agricultural Policy (CAP). The central features of the reform are (i) to bring domestic agriculture support prices closer to world levels over the next three years, (ii) to shift from reliance on subsidies through price supports toward direct income supports, and (iii) to induce a reduction of the area under subsidized food production. The recent CAP reform should contribute to reducing distortions in agriculture, especially if it is sustained and strengthened as part of a dynamic process of agricultural liberalization.

4. A notable feature of industrial country trade policies has been the move toward extension of most-favored-nation (MFN) and/or Generalized System of Preferences (GSP) status to formerly centrally-planned economies. Thus, by April 1992, many OECD countries had granted MFN and/or GSP status to most East European countries, the Baltics, and a number of the states of the former Soviet Union. Several East European countries now face fewer quantitative trade restrictions in many industrial countries. Further progress in this direction by the industrial countries will be important for the trade prospects of East European and other countries.

5. The notable feature of the trade policy stance of many developing countries continues to be unilateral trade liberalization, usually as part of a package of market-opening reform measures and often supported by the Bank and the Fund. These reforms have involved the phased elimination/reduction of quantitative restrictions, replacement of these by tariffs, and a harmonization of the tariff regime to reduce tariff dispersion and move to a lower, more uniform tariff structure. In many cases they have significantly reduced the high degree of complexity and restrictiveness characterizing the pre-reform trade regime. In 1991-92, in addition to the liberalization undertaken in the context of the accessions to the GATT of El Salvador and Guatemala and the disinvocation of GATT Article XVIII:B (trade restrictions for balance of payments reasons) by Argentina, Brazil, Colombia and Peru, new trade liberalization measures were announced or implemented in Eastern Europe and in developing countries in Asia, Africa, and Latin America (for example, Algeria, India, Indonesia, Morocco, Sri Lanka, Tunisia, Uruguay, and Venezuela). In the case of Eastern Europe, the reforms have involved a fundamental reorienting of exchange and trade regimes toward market mechanisms. Similar reforms are being initiated in the countries of the former Soviet Union, as state trading is being replaced by private sector activity and trade is being conducted on the basis of convertible currency. However, export restrictions introduced in response to the differing pace of price liberalization in the various republics and the lack of an efficient payment mechanism point up sharply the transitional difficulties of establishing rapidly a market-based institutional framework to support the desired integration of these countries into the world trading system.

6. Moves toward regional integration have intensified. In Europe, the EC's Single Market Program is making headway as members prepare to eliminate intra-EC barriers; in some instances, however, the replacement of national restrictions by EC-wide measures carries the danger of increasing external restrictions (for example, initial proposals regarding import quotas on bananas from non-preferential suppliers). The European Free Trade Association (EFTA) is preparing for the establishment of the European Economic Area in 1993, and several of its members are seeking accession to the EC.

EFTA and the EC are entering into association agreements with some East European countries providing, inter alia, for eventual establishment of a free trade area with these countries, though "sensitive" sectors such as agriculture are subject to special provisions; trade and cooperation agreements are also being established or discussed with the Baltic states and some of the states of the former Soviet Union. Some East European countries are discussing the establishment of a free trade area, and the Baltic states are studying the prospects of a customs union among themselves. In the Western Hemisphere, negotiations have been completed for the North American Free Trade Agreement (NAFTA) among Canada, Mexico and the United States. The United States also entered into a number of bilateral framework agreements with Latin American countries providing for a gradual removal of barriers to trade in the context of the Enterprise for the Americas Initiative. Examples of other moves toward strengthened integration include the Andean Pact, CACM, Caricom, and Mercosur. In Asia, a framework for the creation of the ASEAN free trade area was recently agreed, while in Africa moves to strengthen regional integration are being pursued including among the PTA, UDEAC, and the West African states1/. Regional trading arrangements can complement the multilateral trading system if they maintain an outward orientation and entail across-the-board intraregional liberalization; the potential for regional blocs to undermine the multilateral system could increase if the Uruguay Round fails.

III. URUGUAY ROUND

7. Since the report to the Spring meeting, the Uruguay Round has been at a virtual standstill. While agreement on a number of elements in the package put forward as the Draft Final Act (DFA) 2/ in December 1991 appears to have solidified, attempts to move forward on the key negotiations on liberalizing market access yielded little over the past few months. The process continues to be blocked by the impasse among major participants on agriculture, despite the progress made in narrowing differences following the CAP reform agreement. While the latter goes a considerable way toward resolving issues with respect to internal support measures, questions remain regarding the volume of subsidized exports and the liberalization of market access.

8. Negotiations have reached the point where only strengthened political resolution can move the process forward. The central outstanding issues include the export regimes and market access in agriculture, the problem of "free-riders" and exclusions in services, and the permissible length of transition periods in the area of intellectual property rights. Other points of difficulty may be resolvable at the negotiators' level, once political accommodation has been reached on the central issues. The recent G-7 Summit in Munich reaffirmed the need for a successful conclusion of the Round in 1992.

1/ CACM = Central American Common Market; Caricom = Caribbean Community; Mercosur = Mercado Comú del Sur; ASEAN = Association of South East Asian Nations; PTA = Preferential Trade Area for Eastern and Southern Africa; UDEAC = Union Douaniere et Economique de l'Afrique Centrale.

2/ The DFA was described in detail in the paper for the Spring 1992 meeting ("Interlinkages between the Policies of the Industrial and Developing Countries, Emphasizing Trade Aspects", DC/92-5, 4/3/92).

9. There is also an increasing public perception (especially on the part of business) of the benefits from the Round and the dangers inherent in failure. In many countries, broad sectors of industry are citing liberalization of market access and the gains in predictability that would flow from a successful Uruguay Round as the reasons why they consider conclusion of the Round a major item on the international economic policy agenda. The positive changes that were put in place in advance of the conclusion of the Round could unravel in the case of further delay. These include consolidation in a multilateral framework of the significant unilateral moves toward trade liberalization in many developing and some industrial countries; streamlining of the GATT's dispute settlement system; and the restraint exercised--albeit only with partial success--during the negotiations on adopting new restrictive measures. The failure of the Round would risk provoking a backtracking on these achievements and a slide toward inward-looking regionalism.

IV. COSTS OF PROTECTION

10. Protection imposes costs on both the protecting country and its trading partners. Estimates of the costs of protection vary widely depending on the coverage, assumptions, and methodology used, and should therefore be used with caution. Most studies have shown that liberalization entails significant welfare gains in the medium to long term, although there may be short-term losses for producers in industries/sectors hitherto sheltered by protection and/or subsidies. It should be noted that many studies only estimate the static gains from trade liberalization, while the dynamic gains are likely to be more significant. Some recent studies investigate the effects of a possible Uruguay Round agreement. A recent OECD Development Center study 1/indicates that under a partial reform scenario of a 30 percent reduction in border measures (assumed to approximate the position in the 1991 Draft Final Act of the Uruguay Round), the global income gain in the year 2002 is $195 billion (in 1992 dollars), of which $104 billion accrues to OECD countries and $91 billion to developing and formerly centrally-planned economies. A complete dismantling of all agricultural protection and industrial tariffs would result in a global income gain of $477 billion, of which $256 billion accrues to OECD countries and $221 billion to developing and formerly centrally-planned economies. Income gains range, for example, from 0.8-3 percent for the EC, EFTA, and Japan; 0.2-0.3 percent for the United States; 0.3-1.5 percent for Latin America; and 2.6-7.9 percent for ASEAN. Some food-importing developing countries could stand to lose initially if food prices rise as estimated--the study emphasizes that potential losses are relatively small in absolute terms and the overall gains are larger, providing room for establishing compensation mechanisms. Fund staff estimates 2/ indicate that removal of manufacturing tariffs of industrial countries could lead to GNP gains for developing countries averaging around 1 1/2 percent a year. Estimates by the World Bank 3/ suggest that a 50 percent reduction in trade barriers by the EC, Japan, and the United States would lead to a $50 billion increase in developing country exports. One study by the ODI 4/ assessed the impact of a Uruguay Round

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1/ Goldin, Ian and Dominique van der Mensbrugghe, Trade Liberalization: What's at Stake? (OECD Development Center: Paris, 1992).

2/ IMF, World Economic Outlook (World Economic and Financial Surveys, October 1990).

3/ World Bank, Global Economic Prospects and the Developing Countries 1992 (World Bank, 1992).

4/ Page, Sheila, Michael Davenport, and Adrian Hewitt, The GATT Uruguay Round: Effects on Developing Countries (ODI: London, 1991).

agreement specifically on different categories of developing countries. Assuming, inter alia, that all MFA quotas are eventually removed and agricultural support is reduced by over 30 percent, developing country exports will rise by 3 percent. The gains accrue entirely to the textile sectors and predominantly to Asian exporters, with the lower gains to African countries partially offset by losses implied by the erosion of preference margins for the African, Caribbean, and Pacific (ACP) countries. These results exclude, however, the impact of any efficiency and income effects from a multilateral agreement. Regarding sectoral effects, a study 1/ of U.S. nontariff barriers (NTBs) on selected industrial goods estimates the costs of protection in terms of welfare foregone to amount to $10 billion per year (in 1984 dollars) each for automobiles and textiles and $1 billion for steel; the annual cost per job protected is estimated to be five times the annual total compensation per worker in the textiles and apparel sector, and 1.7 times in the automobile and steel sectors.

11. The above illustrative estimates understate the importance of reaching agreement in the Uruguay Round, as they only assess the impact of a reduction in current protection levels; in fact, failure to reach agreement is likely to result in increased pressures for protection and eventually higher protection levels with a concomitant loss in welfare.

V. COLLABORATION WITH GATT

12. The Bretton Woods institutions have a long tradition of collaboration with the GATT with which they share common objectives and principles. Well-developed channels of cooperation exist between the staffs. The Director-General of GATT is invited to attend as an observer the ministerial level meetings of the Fund and the Bank. In turn, the Bank and the Fund are represented as observers at sessions of the GATT CONTRACTING PARTIES, the GATT Council of Representatives, and several standing GATT committees. The fact that exchange controls and trade measures can be used as substitutes has from the outset resulted in a special link between the GATT and the Fund, embodied in GATT Articles XIV and XV. Collaboration between the Fund and the GATT has been pursued in terms of the Fund's participation in GATT's consultations with contracting parties maintaining trade restrictions for balance of payments reasons under GATT Articles XII and XVIII:B. Other examples of institutional cooperation include studies prepared by the Fund staff at the request of GATT (for example, on the effects of exchange rate fluctuations on world trade). An inter-agency workshop was recently held under the auspices of the GATT, the UN Statistical Office, and the World Bank to develop a work program aimed at improving the quality of international trade statistics. Efforts continue to improve collaboration among the three institutions.

13. The Fund and the Bank have extended strong support to the Uruguay Round. Fund and Bank staff attend as observers the meetings of selected negotiating groups of the Round. Fund and Bank advice, in the context of use of their resources and in exercising surveillance functions, supports multilateral principles. The deliberations of the Round will have implications for broader collaboration with the Bretton Woods institutions. It is envisaged that the proposed Multilateral Trade Organization (MTO), to be established under the Uruguay Round, will maintain and enhance collaboration with the Bretton Woods institutions. In the area of services the Fund has jurisdiction over the payments side and hence has a direct interest in seeing that any new disciplines developed are consistent with the

1/ de Melo, Jaime, and David Tarr, A General Equilibrium Analysis of U.S. Foreign Trade Policy (MIT Press, 1992).

Fund's jurisdiction. Fund staff have followed closely discussions of the Round's Group on Negotiations on Services (GNS), provided it with technical input on the Fund's role in the services area, and kept in touch with GATT staff on these issues.

14. Surveillance over trade policies is a central role of the GATT (and this function would be carried over to the proposed MTO). At the 1988 mid-term review of the Uruguay Round, participants decided to strengthen surveillance through the establishment of the Trade Policy Review Mechanism (TPRM) under which the trade policy of each member will be periodically examined; final agreement on the TPRM will be part of the final Uruguay Round result. The TPRM became operational in 1989 and has contributed to increased transparency of trade regimes and--through publication of the reviews--to better awareness of the issues among a wider audience. All industrial countries have been under review at least once, while the number of developing countries reviewed is rising. Given their large weight in the world trading system, the Annex gives highlights from the reviews of industrial countries, but is not intended to provide a comprehensive summary of the TPRM reviews.

TRADE POLICIES IN INDUSTRIAL COUNTRIES

This Annex provides highlights of trade policy reviews of industrial countries periodically conducted under GATT's Trade Policy Review Mechanism (TPRM) since 1989, when the TPRM became operational. The write-up below is based on the statements by individual GATT members during the reviews and the documentation for the reviews provided by the GATT secretariat and the country reviewed.

The reviews have recognized that most industrial countries generally had low levels of protection and--with some exceptions--high proportions of GATT-bound tariffs 1/ on industrial products. Protection was concentrated in specific areas and applied, inter alia, through quantitative restrictions, defensive use of antidumping and countervailing duty mechanisms, and unilateral pressure, largely in the form of restraint arrangements; tariff peaks, tariff escalation, 2/ and domestic restrictive market practices were also considered problem areas. The reviews also expressed concern at the high and increasing proportion of the external trade of many industrial countries moving under preferential agreements. Individual countries utilized the opportunity provided by the reviews to explain the working of, and rationale for, their trade regimes and to reiterate their commitment to multilateral liberalization under the Uruguay Round.

Problem areas most frequently singled out in the various country reviews were as follows:

(i) The complexity of the legal and/or tariff systems in some cases (the United States, Canada) diminished an otherwise high degree of transparency and added to the cost of trading; a general lack of transparency was cited in other cases (Japan).

(ii) Subsidies and income supports in agriculture were widely criticized for their breadth and duration, including cases of extensive support (the EC's CAP), selective support (for example, the dairy sector in Canada and the United States), and the smaller producers (EFTA countries, as well as Japan). The reviews also pointed to relatively high levels of assistance to declining industrial sectors (Australia, EC) and increasingly to more dynamic branches such as high technology areas and those with high research and development components (the EC).

(iii) Border protection. Most industrial countries were commended for low tariffs and extensive bindings on industrial products (Canada, the EC, Norway, Sweden, Switzerland, the United States), with only a few having relatively low proportions of bound tariffs (Australia, Finland, New Zealand). Some unilateral liberalization had been undertaken in the context of overall economic deregulation (Australia, New Zealand and Sweden). But continued heavy protection of specific sectors was effected through nonbound tariffs, variable levies and various quantitative restrictions, mainly affecting agricultural products and textiles and clothing. Tariff peaks (especially in agriculture/food sectors) and tariff

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1/ Tariff bindings are obligations undertaken in GATT not to raise tariff rates on specific products above a certain level without compensating reductions in other tariffs.

2/ Tariff escalation refers to a tariff structure such that tariff rates rise with the stage of processing. Tariff peaks are high tariffs well above the average.

escalation (textiles and clothing) were frequent in areas of particular interest to developing countries.

The reviews underscored the increasing resort to managed trade in particular through bilateral agreements in areas such as steel, automobiles, semiconductors and high technology products by both initiators (EC, United States) and acceptors (Japan). While quantitative import restrictions were mainly utilized in the agricultural sector (apart from those contained in the Multi-Fibre Arrangement), resort to import licensing was on the wane in the aftermath of major deregulation efforts (New Zealand).

(iv) Extended use and unpredictable application of antidumping measures and countervailing duties were considered to be problems (EC, United States), as were the unilateral interpretations of antidumping and countervailing duty provisions and nontransparency of both injury review mechanisms and dumping margin determinations. Some countries made little use of such trade measures (Finland, New Zealand, Norway), some had not used them at all (Japan, Switzerland) and at least one (Australia) had reduced recourse to such actions.

(v) Concerns were also expressed about the use of domestic restrictive practices that effectively provided a secondary level of protection, including anticompetitive practices (Japan, Switzerland), cartelization and price surveillance (Austria), and the high degree of freedom of local government in setting standards and providing industry assistance (Australia, Canada, the United States).

PROGRESS REPORT ON THE OUTCOME OF THE UNITED NATIONS CONFERENCE ON ENVIRONMENT AND DEVELOPMENT

(Prepared by Bank staff in consultation with staff of the International Monetary Fund)

I. INTRODUCTION

1. Based on the issues paper "The Interaction of Environment and Development", the Development Committee considered at its last meeting in April the expanding global role of the World Bank in integrating environment and development. In particular, the Committee took note of the stepped-up effort of the World Bank Group in adjusting its existing programs to accommodate environmental concerns, in addressing related concerns in its technical assistance activities, in strengthening its policy dialogue with developing countries, and in deepening its research on sustainable development. In light of the importance of the United Nations Conference on Environment and Development (UNCED), and its implications for the work of the Bank, the Committee requested a progress report on the outcome of the Conference and the follow-up action planned.

2. UNCED took place in Rio de Janeiro, Brazil, from June 3 to June 14, 1992. It was the most representative world conference ever convened and the largest gathering of world leaders ever held (172 countries attended; 115 of which participated at the level of head of state or government). But its lasting significance may well be the process it launched towards a new environmental/ development ethic and the global Plan of Action (Agenda 21) it adopted by consensus to address the challenge of sustainable development.

3. The Conference climaxed a two-year preparatory process carried out under the direction of Messrs. Tommy Koh, Chairman of the Preparatory Committee, and Maurice Strong, Secretary-General of the Conference. The Bank played a major role in the preparations for the Conference. The 1992 World Development Report (WDR) devoted to environment and development, was widely acknowledged as a major analytical contribution to UNCED. Its main message underlines the need to integrate environmental considerations into development policy making. In exploring this two-way relationship, the report argues that strong environmental policies complement and reinforce development; and that continued economic and human development is sustainable and can be consistent with improving environmental conditions, but that this will require major policy, program, and institutional changes.

4. UNCED achieved the following main results:

- Adoption of the Rio Declaration on Environment and Development.
- Endorsement of international conventions on Climate Change and Biodiversity.
- Adoption of a framework of Principles for a Global Consensus on Forests.
- Agreement to negotiate a "Desertification" convention.
- Adoption of Agenda 21.

5. Most observers rated UNCED a success, recognizing that the results reflect the give and take necessary to achieve consensus and that UNCED represents the beginning, not the end, of a long process. As Prime Minister Mrs. Bruntland of Norway, one of the principal architects of UNCED, put it: "We owe it to the world to be frank about what we have achieved here: Progress in many fields, too little progress in most fields, and no progress at all in some fields ... But the direction of where we are heading will have been set."

II. THE PLENARY SESSION

6. The plenary session, in which over 100 heads of state or government took part, provided many useful perspectives on the challenge of UNCED-to governments as well as to multilateral development institutions. A number of recurring themes are noteworthy. Countries agreed that concerted action and shared responsibility are crucial to addressing the linkages between development and environment. The theme of new partnerships, based on shared rights and responsibilities - between donors and aid recipients, and between governments and citizens - was striking in its universality. Nevertheless, there were clear differences among country groups.

7. While supportive of UNCED objectives, developing countries were clearly wary of any potential infringement of their sovereign rights. In addition, they sought clear commitments from industrial countries, especially concerning new, additional, and predictable financial support needed to implement environmental programs, access to environmentally-sound technologies on concessional and preferential terms, and meaningful change in the consumption and production patterns of industrial countries to support sustainable development. Developing countries also expressed concern that the priorities of the developed countries seemed to focus unduly on global issues, in particular, climate change, depletion of the ozone layer and biodiversity, and to under-emphasize national development/environment priorities and poverty reduction. Developed countries, on the other hand, tended to give greater weight to issues of population and more efficient use of existing ODA resources in the stepped-up efforts to address poverty alleviation and global environmental problems.

8. Differences were evident in the approach of developed countries to time-bound commitments to meet the long established ODA targets of 0.7 percent of GNP, as well as specific financial contributions to implementation of Agenda 21. Countries of the Commonwealth of Independent States (CIS) were particularly concerned that their special circumstances as economies in transition should be taken into account in any related obligations of UNCED.

9. Many governments recognized that the UNCED process has been energized by international public opinion mobilized by the independent network of NGOs and by the world's media and that these will play an important follow-up role in monitoring the implementation of Agenda 21. The generally constructive and participatory role played by the NGO community was one of the most striking features of the UNCED preparatory process and of the Conference itself; over 1400 NGOs were formally accredited to the UNCED process.

10. Mr. Preston's statement to the plenary underlined the need for an integrated approach to development, poverty reduction and the environment, and for strong operational linkages between actions to address national environmental issues and related efforts to resolve global problems. It also declared the Bank's readiness to exercise leadership (particularly through the consultative group mechanism, IDA, and the GEF) in helping assemble the substantial additional financial resources required, to help developing countries, particularly the poorest countries, achieve sustainable development.

11. The Managing Director of the Fund also addressed the UNCED plenary and stressed the relationship between economic growth and environmental protection. He indicated that any growth strategy, to be sustainable, must respect the environment, and that environmental protection, to be effective, must be part of a viable growth strategy. In this context, he stressed the importance of the Fund's role in promoting sound economic policy, which facilitates the achievement of environmental objectives.

III. UNCED: THE MAIN RESULTS

12. The Rio Declaration on Environment and Development: The Rio Declaration consists of 27 basic principles designed to guide national and international policies. These principles cover a broad range of issues, including the link between environment and development, the sovereign right of states to exploit their own resources (without damage to others), international cooperation in eradicating poverty, the role of women in sustainable development, and the use of economic instruments in environment/development policy. While the Declaration falls short of the high ideals associated with the UN Declaration on Human Rights (after which it was patterned), its adoption, nevertheless, reflects a commitment - at the highest political levels - to the objectives of UNCED.

13. Conventions on Climate Change and Biodiversity: These conventions, adopted recently by separate International Negotiating Committees, were opened for signature at UNCED; at the end of the Conference, both conventions had been signed by 154 countries. The recent agreement on restructuring the Global Environment Facility (GEF) was instrumental in forging consensus on the designation of the GEF as the interim financial mechanism for meeting developing countries' obligations under both the Climate Change and Biodiversity Conventions.

14. The Climate Change Convention: This convention aims at stabilizing concentrations of greenhouse gases that contribute to global warming. Specifically, it recognizes the need to return to earlier emission levels, suggesting 1990 country levels as a possible benchmark. While the agreement sets approximate deadlines and emission limits, there is no clear-cut link between these two objectives. This seeming ambiguity reflects the opposition by some countries to specific targets and timetables, and to the use of energy taxes for the reduction of greenhouse gases, on the grounds that binding limits would hamper economic growth and competitiveness, and that efficiency measures being introduced are likely to achieve comparable results. The obligations of developing countries to implement their commitments are linked to financial resources and technology made available to them, taking into account their overriding priorities of economic and social development and poverty reduction.

15. The Convention on Biodiversity: This convention has as its main objectives protecting and sustaining the earth's living resources and ecosystems and sharing the benefits from the use of genetic resources. Much of the world's biodiversity lies within developing countries, while the biotechnology industry that exploits these resources is located in developed countries. Thus, issues of control over access and adequate returns to developing countries were central to the negotiations. Among the central features of the treaty are: (i) the provision of financial and technical support by developed countries to help developing countries conserve their living resources; and (ii) the equitable sharing of the results of

biotechnological research and development between investors and developing countries from which the research originated. While a number of developed countries expressed reservations on grounds of inadequate control over the use of financial resources provided and patent protection for investors, only the United States has indicated its intention not to sign the treaty.

16. Principles for a Global Consensus on Forests: Agreement on a framework of forest principles was reached after prolonged and contentious negotiations. The guiding objective of these principles is to reconcile the potentially conflicting objectives of fostering sound management, conservation and development of all types of forests, taking into account traditional uses as well as the potential for development through sustainable forest management.

17. Desertification Convention: UNCED agreed to request the General Assembly, at its next session in September, to establish an intergovernmental committee to negotiate an international convention to combat desertification, particularly in Africa.

18. Agenda 21: The main operational product of UNCED, Agenda 21, is an ambitious action plan covering over 100 program areas (e.g. climate, marine pollution, desertification, human resources, sustainable agriculture) integrating environment and development, to be supported by new and additional financial resources, improved access on favorable terms to environmentally-sound technology, and strengthened institutional capacity in developing countries. States were called upon to prepare national sustainable development plans outlining their own environmental problems as well as their strategies, programs, and priorities for implementing Agenda 21. UNCED agreed that external financing should be assembled to support these programs through a variety of existing, rather than new funding mechanisms. These funding sources would include the multilateral development banks, including regional development banks, a restructured GEF, bilateral assistance programs, including debt relief, and voluntary contributions through NGO channels which currently represent about 10 percent of total ODA. Agenda 21 also calls for exploring innovative ways to generate new public and private flows, in particular various forms of debt relief, including greater use of debt swaps, economic and fiscal incentives, the feasibility of tradeable permits, new schemes for fund raising through private and non-governmental channels, and reallocation of military resources to development. Existing aid consortia, consultative groups and round tables were asked to support these country-based programs by integrating environment and development assistance strategies, by mobilizing new and additional resources, by making most effective use of existing resources, and by adjusting their membership and operations to facilitate this process.

19. Concerning the funding of Agenda 21 and other outcomes of the Conference, UNCED called for new and additional resources to be maximized, using all available funding sources and mechanisms. In this connection, it underlined the important role to be played by IDA in implementing Agenda 21 and urged that "among various issues and options that IDA Deputies will examine in the forthcoming 10th replenishment, special consideration should be given to the statement made by the President of the World Bank at the Conference in the plenary meeting in order to help the poorest countries meet their sustainable development objectives." UNCED also endorsed the plan to restructure the GEF, and agreed that it was the proper mechanism to cover the incremental costs of relevant activities for achieving global benefits under Agenda 21.

20. The main principles on which restructuring of the GEF will be carried out were agreed upon at the last meeting of participants held on April 29-30, 1992. While its basic mission will be to continue providing concessional and additional funding of agreed incremental costs for achieving global environmental benefits in its four focal areas (limiting emissions of greenhouse gases, preserving biodiversity, protecting international waters, protecting the ozone layer) a restructured GEF would:

- support activities related to land degradation issues (primarily desertification and deforestation) as they relate to the four focal areas;
- assure the cost-effectiveness of its activities in addressing the targeted global environmental issues;
- fund programs and projects which are country-driven and consistent with national priorities designed to support sustainable development:
- become transparent and accountable to contributors and beneficiaries alike; and
- develop sufficient flexibility to introduce modifications as the need arises.

Governance of the restructured GEF would reflect these principles; universal participation is seen as key to the Facility's success.

21. Institutional arrangements for effective follow-up of the Conference provide for establishment by the UN General Assembly of a Sustainable Development Commission. The Commission will provide a high-level inter-governmental forum to monitor progress by governments and international agencies (including multilateral financial institutions) in implementing Agenda 21 and the environmental conventions. It will also consider issues contained in the national sustainable development reports provided by governments (for example, problems related to financial resources or technology transfer), and foster coordination through the active involvement in its work of relevant organizations of the UN system and NGOs.

22. During its next session in September, the UN General Assembly will determine organizational and operational modalities of the Commission which would report to a "revitalized" Economic and Social Council. Membership would consist of states elected "with due regard to geographical distribution", and would be supported by a high-quality secretariat under the direction of the UN Secretary-General.

IV. PARALLEL EVENTS

23. In addition to the formal meetings, there were numerous events sponsored by the independent sectors. Particularly noteworthy was the NGO-sponsored "Global Forum 92", where both GEF and World Bank were among the hundreds of exhibitors. Technical staff made well-received

presentations on WDR 1992, GEF, and related Bank policies (e.g. urban, industry, poverty, environment, participatory development) to a variety of groups representing business, industry, local officials, women, youth, indigenous people and broad-based NGO development interests. Press briefings on the Bank's environment and development agenda, and on the GEF were also held.

V. FOLLOW-UP BY THE WORLD BANK

24. The Bank's expanding global role in integrating environment and development has been strengthened by the agreements reached at UNCED. In addition, the Conference provided an extensive feedback on related Bank policies and actions by multiple constituencies present at Rio de Janeiro. A substantial work program lies ahead in implementing the restructuring of the GEF; more systematically building into the Bank's operational activities the findings of WDR 92; helping developing countries, in particular, the poorest countries, define their environmental objectives; and mobilizing the necessary resources for their implementation, including strengthening the role of the consultative group mechanism. Within the wider UN system, the Bank will participate actively in the Task Force on Environment and Development recently created by the UN Secretary-General (chaired by Mr. Edouard Saouma, Director-General of FAO) which will consider guidelines for the inter-agency division of labor in implementing Agenda 21, including arrangements to improve coordination, and UN system reporting to the proposed Sustainable Development Commission.

VI. ROLE OF THE IMF

25. The current direction of the Fund's work is supportive of Agenda 21. The Fund continues to advise member countries on macroeconomic policies which, among other things, encourage them to create market-based pricing and open exchange and trade systems. To the extent that market prices fail to reflect environmental externalities, price-oriented approaches (including taxation policies) to reduce negative externalities are more efficient than direct controls or quantitative restrictions. These are inherently conducive to optimal resource use, including a more economic use of depletable resources and safeguarding of the environment. In addition, the Fund has allocated staff resources to liaise with other organizations (such as the World Bank, UNEP and the OECD and national governments) with environmental competence and responsibilities and to monitor relevant research. The aim is to ensure that appropriate material produced outside the Fund is disseminated within the Fund in support of the Fund's operational work, thereby contributing to understanding of the impact of macroeconomic policy instruments on the environment. Increasing this understanding is consistent with Agenda 21 which encourages national authorities to consider the environmental aspects of their macroeconomic policies. Equally, to the extent that Agenda 21 contains various proposals for domestic action that have financial implications, the staff will need to consider these with national authorities to ensure their consistency with the macro-policy framework aimed at promoting balanced and sustainable growth.

DEVELOPMENT COMMITTEE

JOINT MINISTERIAL COMMITTEE
OF THE
BOARDS OF GOVERNORS OF THE BANK AND THE FUND
ON THE
TRANSFER OF REAL RESOURCES TO DEVELOPING COUNTRIES

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September 21, 1992

COMMUNIQUE

1. The Development Committee held its 44th meeting in Washington DC, on September 21, 1992, under the chairmanship of Mr. Alejandro Foxley, Minister of Finance of Chile. 1/ After reviewing the world economic scene, this meeting concentrated on ways of increasing resources for development. The Committee welcomed the new members who have joined the Bank and the Fund since their last meeting.

2. DEVELOPMENT OBJECTIVES. Ministers recalled their agreement at their meeting in Bangkok on the development objectives of the nineties: the reduction of poverty and the achievement of sustainable growth, actions to protect the environment being essential to both objectives. They reviewed the resources necessary to reach these objectives, and the actions which would be necessary to increase their volume and effectiveness.

3. DOMESTIC RESOURCES. They noted that most developing countries 2/ fund the major part of their investment from domestic savings, both public and private. They concluded therefore that the top priority is for developing countries wherever possible to increase the volume of these savings and the effectiveness of their use. This will require the adoption and maintenance of appropriate macroeconomic policies; reduction in wasteful and unproductive programs; and efficient financial and banking systems.

1/ Mr. Lewis T. Preston, President of the World Bank, Mr. Michel Camdessus, Managing Director of the International Monetary Fund, Mr. Ahmadu Abubakar, Minister of Finance of Nigeria and Chairman of the Group of 24, and Mr. Peter Mountfield, Executive Secretary, participated in the meeting. Observers from a number of other international and regional organizations and from Switzerland also attended.

2/ In the rest of this Communique the phrase "developing countries" includes economies in transition.

4. TRADE. Ministers agreed that a much more open world trading system would be beneficial to all countries but is of the utmost importance to the developing countries. In the context of resource flows, developing countries need to increase earnings from trade, in order to finance imports, service debt and to promote sustainable domestic economic growth. Increased export opportunities will also make developing countries more attractive to investors. They therefore emphasized once again the need for rapid agreement on the outstanding issues in the Uruguay Round, noting that this would lead to a broader, more liberal and more stable trading system, and extend market access for many developing countries. They agreed that regional trade arrangements should emphasize trade-creation rather than trade-diversion, consistent with multilateral principles, and should ensure trade opportunities for developing countries.

5. FOREIGN INVESTMENT. For most developing countries, earnings from trade must be supplemented by external resources. For a growing number of them, a large part of these resources is now provided by private foreign investors in the form of direct foreign investment. Ministers noted the recent increase in portfolio investment, while recognizing that its higher liquidity made its impact different from FDI. Ministers considered the measures necessary to attract more private flows, and concluded that the measures which promote domestic investment are likely also to attract foreign investors and the return of flight capital. They concluded that the maintenance of macroeconomic stability and the creation of a climate favorable to enterprise are essential, both to attract more investment and to increase the number of countries receiving foreign flows.

6. INVESTMENT GUIDELINES. Additional measures may be needed to attract foreign investment. The creation and maintenance of a suitable legal framework can be an important part of this process. Ministers therefore reviewed with interest the Investment Guidelines which will shortly be published, together with an explanatory commentary, and calls them to the attention of member countries. These Guidelines have been prepared at the request of the Development Committee to promote fair and equitable international standards for the general treatment of all foreign direct investment in the absence of applicable treaties, and should be of particular value to developing countries. Ministers expect the Guidelines to serve as an important step in the progressive development of international practice in this area and hope that they will facilitate further developments through bilateral treaties and similar instruments. They also noted the related work being undertaken in other fora to develop principles for the conduct of foreign investors.

7. COMMERCIAL BANK AND MARKET LENDING. Ministers welcomed the increasing access of certain developing countries to the international financial markets, especially by those which are implementing sustainable economic reforms, and have entered into debt and debt-service agreements with the commercial banks. They considered that some increase in the volume of trade finance and project lending provided by the banks may occur, but noted that commercial bank lending to developing countries was unlikely to return to previous levels. They noted the active role taken by the Inter-American

Development Bank and other regional banks in promoting effective investment reforms which are essential for nurturing a stable financial environment. They believed that the international financial institutions should continue to encourage the efficient mobilization of financial resources by promoting effective investment reforms, privatization and financial sector reforms. Ministers noted the improved economic performance achieved by the developing countries following the implementation of debt and debt-service reduction and therefore encouraged the timely conclusion of negotiations between other countries and their commercial banks.

8. INCREASING NONCONCESSIONAL FLOWS. Ministers agreed to review at their next meeting the prospects for increasing the flows of private resources, and improving the access of developing countries to global markets for loan and equity capital. Members agreed on the need to gather accurate and timely information on the stocks and flows of private capital to developing countries and to assess the implications of these developments. They asked the Bank and the Fund to prepare a joint paper for this purpose which would also include the role of the international financial institutions in promoting and catalyzing such flows and the extent of any remaining obstacles placed by developing and industrial countries to resource flows.

9. DEBT. Ministers recognized that the efforts of many developing countries need to be supported by rescheduling and, in some cases, by debt and debt service reduction measures, both public and private. Ministers welcomed the progress in the international debt strategy, including arrangements this year with Argentina, Bolivia, and Brazil among others. Such arrangements have now been reached with 12 countries and account for more than 90 per cent of the commercial bank debt of the major debtor nations. They urged the Paris Club to recognize the special situation of some highly indebted lower-middle income countries on a case-by-case basis. Ministers also welcomed the enhanced debt relief extended to the poorest countries by the Paris Club, noting that the Paris Club has agreed to consider the stock of debt, under certain conditions, after a period of three to four years. They invited the Paris Club to maintain its continuing review of the debt strategy. They acknowledged the continued need of support for heavily-indebted countries which by adopting strong adjustment policies have avoided rescheduling.

10. BILATERAL AID. Poorer developing countries will continue to require substantial concessional assistance for many years. A number of additional countries have recently become potential recipients of aid, while new requirements, especially in the environmental field, have added to the needs. The Committee noted that the World Bank and the IMF believe that an increased volume of external resources, to complement the efforts of the developing countries, will be crucial to meeting those needs. Ministers therefore invited bilateral donors to increase their assistance, particularly for countries that are sustaining sound policies, as circumstances permit, especially those whose aid programs are still below 0.7% of GNP, and welcomed the contribution of those whose aid is substantially above that level. They stressed the need for donors and recipients to emphasize the

quality and effectiveness of aid, and for an increased proportion to be directed toward improving the living conditions of the poor, and to the poorest countries and those with a strong commitment to poverty reduction.

11. MULTILATERAL FLOWS. Ministers recognized the need for multilateral action to complement that of bilateral donors. They noted the ongoing negotiations over the Tenth Replenishment of IDA. They urged the IDA Deputies to make significant progress at their meeting in November 1992 so as to secure agreement by the end of the year on a substantial IDA-10 replenishment. Ministers also agreed that continuing consideration should be given to an Earth Increment for environmental purposes. They welcomed the extension to November 1993 of the period for commitments under the Fund's enhanced structural adjustment facility (ESAF) and the Executive Board's intention to review the effectiveness of ESAF programs and examine the options and operational modalities of a possible successor facility. They urged that this work be completed in good time before November 1993. They welcomed the Bank's assurance that the current capital base of the IBRD is sufficient to sustain and enhance the volume of lending to existing borrowing members, while providing substantial support for the economic reform and adjustment efforts of the countries of the former Soviet Union. Ministers agreed to review the effectiveness of the Bank's lending at a future meeting.

12. ENVIRONMENT. Ministers welcomed the wide-ranging consensus reached at the United Nations Conference on Environment and Development. They recognized the ongoing financing needs associated with Agenda 21. They also noted that UNCED called for additional funding to be channeled through existing institutions, including the Global Environment Facility, which will be restructured on lines to be agreed by the participants. Ministers urged the World Bank to play a full part in carrying forward the results of UNCED in collaboration with other agencies in the UN system and to the regional banks, and to report progress to the Committee at its meeting in September 1993.

13. DROUGHT, FAMINE AND WAR. The Committee noted with great concern the problems of drought in Southern and Eastern Africa, the severe famine in Somalia, widespread flooding in the Indian subcontinent and the problems of several war-affected countries. They welcomed the coordinated international action now under way to alleviate suffering in many of these areas, and called for the active cooperation of all governments and agencies concerned, both to overcome the immediate problems and to lay the foundations for future recovery and development.

14. DEPARTURE OF CHAIRMAN. The Committee placed on record its special appreciation of the distinguished record of Mr. Alejandro Foxley during his two years as its Chairman.

15. SPRING MEETING. The Committee agreed to meet again in Washington DC on May 1, 1993.

REPORT TO THE BOARDS OF GOVERNORS OF THE
IMF AND THE WORLD BANK BY THE
HON. ALEJANDRO FOXLEY,
CHAIRMAN OF THE JOINT MINISTERIAL COMMITTEE
OF THE BOARDS OF GOVERNORS ON THE TRANSFER
OF REAL RESOURCES TO DEVELOPING COUNTRIES
(Development Committee)

Annual Meetings-1992

The Development Committee met twice during the year under review and discussed a broad range of development issues.

1. We started with a very wide-ranging debate on Development Priorities for the 1990s. The Committee agreed that the priority objectives were: (i) the reduction of poverty, and (ii) the achievement of sustainable growth. They also agreed that actions to protect the environment were essential for both objectives and stressed that the main task was now to implement those objectives. There was a remarkably wide consensus on what needs to be done -- a wider consensus than we could have attained even five years ago.

a. The Committee agreed that success in meeting these objectives will depend on the economic policies pursued by both developing and industrial countries, the creation of a market-friendly environment; the strength of developing country human resources; availability of human resources as well as the complementary roles of the public and private sectors. Ministers recognized the need to pursue further growth-oriented economic reforms in order to mobilize domestic resources, attract FDI and increase the efficiency of capital use. The Committee called on the World Bank and the IMF to continue to consider how best they could support the reform efforts of adjusting countries which were facing short-term problems requiring appropriate safety nets.

b. The Committee underlined that economic reform in the developing countries should be complemented by improvements in the trade, energy, industrial and agricultural policies of the industrial countries. In particular, the Committee recognized that a wider access to world markets was essential. Ministers were therefore disturbed at the continuing delay in the Uruguay Round and emphasized the urgent need for a successful conclusion.

c. The Committee urged that every effort should be made to increase ODA flows where needed, especially now that a lessening in international tension allows a reduction in military expenditure. Ministers acknowledged that the creditor nations could continue to make progress in dealing with the debt overhang.

d. The Committee urged the Governors to approve the $1 billion capital increase for IFC. Ministers recognized the need for IDA Deputies to reach agreement by the end of 1992 on IDA-10, preferably at a level substantially above that of IDA-9. Ministers agreed on the importance of private sector development as one of the priorities for the World Bank Group. Some of our Members are very concerned that in recent years net transfers from the World Bank to the totality of developing countries have turned negative. In order to sustain development efforts, the Committee stressed the need to maintain positive net transfers to countries which are still in the adjustment process. It was this debate which led us to look again at the totality of resource transfers to developing countries, a topic which we debated on Monday. Ministers welcomed the states of the former USSR into the Bretton Woods institutions and noted the World Bank's assurance that its assistance to Eastern and Central Europe could be accomplished while continuing to support the efforts of its traditional borrowing members.

The Committee welcomed the recent expansion in the list of ESAF-eligible countries, and the IMF's operations in support of adjustment efforts. Ministers urged those countries which had not approved the Fund quota increase package to act speedily.

2. Turning from general objectives to particular operations, Human Resource Development (HRD) was the second main issue. The Committee reaffirmed the World Bank's conclusion that HRD is at the heart of any strategy for attaining the agreed objectives of reducing poverty and spurring economic growth. They stressed that in order to achieve these objectives donors and recipients need to cooperate in the social field.

Concerning the Bretton Woods institutions, the Committee endorsed the recent shift in the pattern of World Bank lending and the projections for FY92-94 which show an increased share (from about 6 per cent in the early 1980s to about 15 percent) going to HRD. The Committee also encouraged the IMF to continue to increase its emphasis on the social aspects of adjustment.

3. As I reported to you last year, the Committee has decided to carry out an annual review of the interlinkages between policies of industrial and developing countries. Such review focussed on trade. While welcoming the significant efforts made by many developing countries to undertake trade reform and open up their markets, Ministers encouraged industrial countries to complement this by accelerating the pace of their liberalization efforts.

Ministers once more urged all participants to recognize the international importance of the Uruguay Round, and to work urgently for an outcome which would result in a substantial reduction of trade barriers.

Ministers recognized the need to control potential damage to the environment but agreed that such legitimate concerns should not be used by any country to justify new or existing barriers to trade.

We also suggested that the World Bank and the IMF should undertake and publish regular assessments of the impact on developing counttries of changes in world trade patterns; the institutions should continue to support the efforts of developing countries in this area, and to collaborate with the GATT in promoting open trade policies.

5. The final issue was the interaction between environment and development policies in preparation for the UNCED Rio Conference.

The Committee recognized that economic growth and human development can be consistent with improving environmental conditions, but that this would require significant policy, program and institutional changes in dealing with national and global environmental problems.

While specifying the elements of a strategy at the national level, Ministers recognized that many developing countries would continue to need increased external help to tackle national environmental problems and agreed that official support should be provided through existing development institutions rather than by setting up a separate Green Fund.

Ministers believe that the Global Environment Facility (GEF) should play a leading role in providing new and additional financial resources, and its governance should ensure effective representation and participation by all countries. The Committee asked the GEF participants to reach early decisions on the future coverage, governance and financing of the GEF; of course this has now been done. Ministers welcomed the World Bank's account of its own environmental activities, and the related activities of the IMF. Ministers also agreed that consideration should be given to a special "Earth Increment" to IDA-10; as you know, those negotiations are still continuing.

5. Concluding Remarks

Mr. Chairman, this is the last meeting of my two-year tenure. I want to end these remarks by thanking the Members and Observers of the Development Committee for their valuable contributions to our discussions. I also would like to thank the Bretton Woods Institutions and their respective heads for their unwavering support of our activities.

Appendix A. Agenda for the 44th Meeting of the Development Committee
Washington, D.C., September 21, 1992

1. Main Papers for discussion:

   (a) Resource Flows and Transfers to the Developing Countries; 1/

   (b) Legal Framework for the Treatment of Foreign Investment. 2/

2. Progress Reports: (To take note)

   (a) Recent Developments in the Uruguay Round; 3/

   (b) Outcome of the United Nations Conference on Environment and Development and the Follow-up Action Planned; 4/

   (c) Status of the Negotiations on the Tenth Replenishment of the International Development Association (IDA). 5/

3. Other Business

Notes

1/ This paper, to be prepared by the World Bank and the IMF, responds to the request in paragraph 3 of the October 1991 communique, and in the last section of the April 1992 communique.

2/ This paper relates to a request to the World Bank Group in paragraph 8 of the April 1991 communique, and in the last section of the April 1992 communique.

3/ This progress report, to be prepared by the World Bank and the IMF, responds to the request in the first section of the April 1992 communique.

4/ This progress report will be prepared by the World Bank in consultation with the IMF, as requested in the second section of the April 1992 communique.

5/ The President's Report will include a section on this topic.

Appendix B. Members of the Development Committee
(List of Countries Represented by them and their Executive Directors at the World Bank and the International Monetary Fund:
(September 19, 1992)

Members	Executive Directors	Countries
1. Mohammad Abalkhail Minister of Finance and National Economy Saudi Arabia Alternate Member: Hamad Al-Sayari Governor Saudi Arabian Monetary Agency Saudi Arabia	Ibrahim A. Al-Assaf (Bank) Muhammad Al-Jasser (Fund)	Saudi Arabia
2. Ibrahim Abdul Karim Minister of Finance and National Economy Bahrain	Fawzi Hamad Al-Sultan (Bank) Mohamed Finaish (Fund)	Bahrain, Egypt, Jordan, Kuwait, Lebanon, Maldives, Oman, Pakistan, Qatar, Syrian Arab Republic, United Arab Emirates, Republic of Yemen
3. Anwar Ibrahim Minister of Finance Malaysia	Aris Othman (Bank) J.E. Ismael (Fund)	Fiji, Indonesia, Lao People's Democratic Republic, Malaysia, Myanmar, Nepal, Singapore, Thailand, Tonga, Viet Nam
4. Piero Barucci Minister of the Treasury Italy	Rosario Bonavoglia (Bank) Renato Filosa (Fund)	Greece, Italy, Malta, Poland, Portugal (Albania)
5. Mohamed Berrada Minister of Finance Morocco	Mohamed Benhocine (Bank) Abbas Mirakhor (Fund)	Afghanistan, Algeria, Ghana, Islamic Republic of Iran, Socialist People's Libyan Arab Jamahiriya, Morocco, Tunisia
6. Nicholas F. Brady Secretary of the Treasury United States	E. Patrick Coady (Bank) Thomas C. Dawson II (Fund)	United States
7. Alemayehu Daba Acting Minister of Finance Ethiopia	Jabez Ayo Langley (Bank) L.B. Monyake (Fund)	Angola, Botswana, Burundi, Ethiopia, The Gambia, Guinea, Kenya, Lesotho, Liberia, Malawi, Mozambique, Namibia, Nigeria, Seychelles, Sierra Leone, Sudan, Swaziland, Tanzania, Uganda, Zambia, Zimbabwe
8. John Dawkins Treasurer Australia	John H. Cosgrove (Bank) E.A. Evans (Fund)	Australia, Kiribati, Korea, New Zealand, Papua New Guinea, Solomon Islands, Vanuatu, Western Samoa (Marshall Islands, Mongolia)

Members	Executive Directors	Countries
9. Kablan D. Duncan Minister Delegate to the Prime Minister in charge of Economy, Finance, Commerce and Planning Cote d'Ivoire	Jean-Pierre Le Bouder (Bank) Corentino V. Santos (Fund)	Benin, Burkina Faso, Cameroon, Cape Verde, Central African Republic, Chad, Comoros, Republic of Congo, Cote d'Ivoire, Djibouti, Equatorial Guinea, Gabon, Guinea-Bissau, Madagascar, Mali, Mauritania, Mauritius, Niger, Rwanda, Sao Tome and Principe, Senegal, Somalia, Togo, Zaire
10. Alejandro Foxley Minister of Finance Chile Alternate Member: Juan J. Diaz Perez Minister of Finance Paraguay	Felix Alberto Camarasa (Bank) Alejandro Vegh (Fund)	Argentina, Bolivia, Chile, Paraguay, Peru, Uruguay
11. Tsutomu Hata Minister of Finance Japan	Yasuyuki Kawahara (Bank) Hiroo Fukui (Fund)	Japan
12. W. Kok Deputy Prime Minister and Minister of Finance Netherlands Alternate Member: J.P. Pronk Minister for Development Cooper Ministry of Foreign Affairs Netherlands	Eveline Herfkens (Bank) G.A. Posthumus (Fund)	Bulgaria, Cyprus, Israel, Netherlands, Romania, Yugoslavia (Georgia, Moldova, Ukraine
13. Norman Lamont Chancellor of the Exchequer United Kingdom	David Peretz (Bank and Fund)	United Kingdom
14. Philippe Maystadt Minister of Finance Belgium	Bernard Snoy (Bank) Jacques de Groote (Fund)	Austria, Belgium, Czechoslovakia Hungary, Luxembourg, Turkey (Belarus, Kazakhstan)
15. Donald Mazankowski Deputy Prime Minister and Minister of Finance Canada	Frank Potter (Bank) C. Scott Clark (Fund)	Antigua and Barbuda, The Bahamas, Barbados, Belize, Canada, Dominica, Grenada, Guyana, Ireland, Jamaica, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines

Members	Executive Directors	Countries
16. Wendell Mottley Minister of Finance Trinidad and Tobago	Ernest Leung (Bank) Alexandre Kafka (Fund)	Brazil, Colombia, Dominican Republic, Ecuador, Haiti, Philippines, Suriname, Trinidad and Tobago
17. Michel Sapin Minister of Economy and Finance France	Jean-Pierre Landau (Bank and Fund)	France
18. Manmohan Singh Minister of Finance India	J.S. Baijal (Bank) G.K. Arora (Fund)	Bangladesh, Bhutan, India, Sri Lanka
19. Carlos Solchaga Minister of Economy and Finance Spain	Moises Naim (Bank) Angel Torres (Fund)	Costa Rica, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Spain, Venezuela
20. Carl-Dieter Spranger Federal Minister for Economic Cooperation Germany	Fritz Fischer (Bank) Bernd Goos (Fund)	Germany
21. Wang Bingqian State Councillor and Minister of Finance China	Wang Liansheng (Bank) Che Peiqin (Fund)	China
22. Anne Wibble Minister of Finance Sweden	Jorunn Maehlum (Bank) Ingimundur Fridriksson (Fund)	Denmark, Finland, Iceland, Norway, Sweden (Estonia, Latvia, Lithuania)

Alternate Member:

Sigbjoern Johnsen
Minister of Finance
Norway

Appendix C. Observers to the Development Committee

African Development Bank	(AfDB)
Associate: Arab Bank for Economic Development in Africa	(BADEA)
Arab Fund for Economic and Social Development	(AFESD)
Asian Development Bank	(AsDB)
Commission of the European Communities	(CEC)
Associate: European Investment Bank	(EIB)
Commonwealth Secretariat	(COMSEC)
General Agreement on Tariffs and Trade	(GATT)
Inter-American Development Bank	(IDB)
International Fund for Agricultural Development	(IFAD)
Islamic Development Bank	(IsDB)
Organisation for Economic Co-operation and Development	(OECD)
Associate: Development Assistance Committee	(DAC)
OPEC Fund for International Development	(OPEC FUND)
United Nations	(UN)
Associates: UNCTAD UNDP	(UNCTAD) (UNDP)
Switzerland	(SWITZERLAND)

Appendix D. Authors of the Development Committee Papers

	Title of Papers	Author
1.	Issues paper on "Resource Flows to Developing Countries" (prepared jointly by staff of the World Bank and International Monetary Fund)	Ronald Johannes, IECDI Kwang Jun, IECDI World Bank Anthony R. Boote Charles V.A. Collyns Michael G. Kuhn IMF
2.	Legal Framework for the Treatment of Foreign Investment	This report was prepared by a task force consisting of the General Counsel of the World Bank (IBRD and IDA), IFC and MIGA, and chaired by Mr. Ibrahim F.I. Shihata, Vice President and General Counsel
3.	Progress Report on "The Outcome of the United Nations Conference on Environment and Development	Carlston Boucher, EXTIE Jane Pratt, EXTDR World Bank
4.	Progress Report on "Trade Policy Developments" (prepared jointly by the staff of the World Bank and the International Monetary Fund	Patrick Low, IECIT World Bank Naheed Kirmani and Joslin Landell-Mills IMF

Joint Ministerial Committee of the Boards of Governors
of the World Bank and the International Monetary Fund
on the Transfer of Real Resources to Developing Countries
(Development Committee)

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