Review of World Bank Conditionality

Operation Policies and Country Services
Country Economics
September 21, 2005
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Objectives of the Review

- Document the evolution of the Bank's approach to conditionality
- Take stock of how lessons of experience have been reflected in recent trends
- Take a fresh look at the Bank’s own practice of conditionality
- Lead to a set of good practice principles for the Bank’s support for policy-based programs
Issues

How to reconcile tensions between:

- country ownership vs. donors’ need for fiduciary accountability/development effectiveness?
- predictability of resource flows vs. performance orientation?
- flexibility vs. results-focused, transparent implementation framework?
Five Main Messages

- The **operational policy** introduced in 2004 is consistent with a view that conditionality is neither coercion to undertake reform, nor prescriptive of policy content;

- The Bank has fully recognized the importance of **country ownership** for development effectiveness—like other donors, it is grappling with the practical challenges of assessing ownership and responding to changing policy environments;
Five Main Messages (cont’d)

- The Bank has made important strides in adapting its policy-based lending to complex reform programs and focusing on critical actions, but should try **avoid using large and complex policy matrices** – especially in multi-sectoral operations;

- The Bank’s conditions and expected prior actions (triggers) have typically been transparently disclosed and clearly defined. However, the flexibility of programmatic approaches needs to be exercised cautiously to **balance predictability with performance**;
Five Main Messages (cont’d)

- The Bank’s approach is fully compatible with the goal of harmonizing financial support with other development partners while retaining the Bank’s distinct accountability.
Modalities

The Bank applies Conditionality in a variety of settings:

- Prior actions and tranche-release conditions
- Triggers
- Benchmarks
Modalities (cont’d)

- **Prior Actions**: critical conditions that must be met prior to a single-tranche operation becoming effective;

- **Tranche-release conditions**: for multi-tranche operations, these must be satisfied before a tranche can be released, and are in addition to those conditions required for board presentation.

- These conditions are specified in a schedule to the legal agreement.
Modalities (cont’d)

Benchmarks:

- Describe the government’s program in areas monitored by the Bank;
- Often small steps in the reform process that represent significant progress markers.
- Benchmarks are not conditions as they are not determinative of disbursements and are not included in the legal agreement.
Modalities (cont’d)

Triggers:
- An important component in programmatic lending
- The represent a notional set of expected prior actions for future operations
- Allow flexibility to adapt to a changing program environment
- Triggers are not conditions as they are not determinative of disbursements and are not included in the legal agreement.
Trends: Content

- Content of policy-based lending has shifted from short-term economic management to complex medium-term institutional reforms
- Strong emphasis on public sector/governance

Source: ALCID, World Bank
Trends: Content

- **Public sector governance** conditionality has grown in importance.
  - This trend corresponds to a stronger attention to improved alignment of resources with development priorities and to the efficiency of resource use.

- The emphasis on **privatization** has declined since the 1990s.
  - The shift away from privatization is also related to the increased attention to the quality of the investment climate as a whole.
  - In noncompetitive sectors, the institutional framework has become central to the design of reforms.
Trends: Content

- **Conditionality on user fees** is extremely limited
  - Where used, conditions figure more prominently in the power sector (Eastern Europe and Latin America),
  - There are virtually no conditions in health, education, and water.

- **Conditionality on trade** has declined significantly since the mid-1980s.
  - Conditions now account for less than 2 percent of the total number of conditions.
  - Current focus is on institutional issues, such as the performance of customs agencies, product quality, and certification.
Trends: Number of Conditions

- Conditionality has been declining for over a decade …

*Trends in World Bank Conditions, FY80-05*

*Source: ALCID, World Bank.*
Trends: Number of Conditions

... but indicative benchmarks have been rising, mainly because of multisector programmatic loans ...

Source: ALCID, World Bank.
Trends: Indicative Benchmarks

… IDA credits account for most of the increase in indicative benchmarks

Source: ALCID, World Bank.
Trends: Coverage

- The average number of policy areas covered in programmatic IDA credits has been increasing—reflecting the multisectoral nature of PRSCs.

![Bar chart showing trends in Programmatic and Non-Programmatic IDA credits from FY00 to FY05.](source.png)

Source: ALCID, World Bank.
Trends: Coverage

- The number of policy areas increases in subsequent programmatic series

<table>
<thead>
<tr>
<th></th>
<th>PRSC I</th>
<th>PRSC II</th>
<th>PRSC III</th>
<th>PRSC IV</th>
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<td>PRSC I</td>
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<tr>
<td>PRSC II</td>
<td>6</td>
<td>5</td>
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<tr>
<td>PRSC III</td>
<td>6</td>
<td>6</td>
<td>6</td>
<td>9</td>
<td>Vietnam</td>
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</table>

Source: ALCID, World Bank
Trends: Approaches to Conditionality

- Programmatic loans have fewer conditions than non-programmatic loans, but more indicative benchmarks.

Source: ALCID, World Bank
Trends: Selectivity

- Better performing IBRD countries: More conditionality and indicative benchmarks on average

- Better performing IDA countries: Less conditionality, but more indicative benchmarks

Source: ALCID, World Bank
Trends: Predictability and Higher Volumes of DPL Disbursements

Red dotted line indicates start of PRSC program
What has happened to aggregate Bank-Fund conditionality?

Reduced burden?
- Overall reduction of aggregate conditionality critical for disbursement (more so for MICs than for LICs)

Gaps in coverage?
- No evidence
- Apart from conditionality, Fund and Bank engage through analytic work, technical assistance, etc.
- Bank reduced the number of critical actions in its PRSCs but reflected policy dialogue with greater coverage of benchmarks in policy matrices

Remaining challenges
- Interpretation of lead agency concept and criticality in practice
- Institutional differences between the Fund and the Bank
- Aggregate conditionality in broader context of donor harmonization
Aggregate Conditionality: MICs (including WB benchmarks)

* Number of IMF and WB conditions per program year

Source: MONA (IMF) and ALCID (World Bank).
Aggregate Conditionality: LICs

* Number of IMF and WB conditions per program year

Source: MONA (IMF) and ALCID (World Bank).
Good Practice Principles
1. Reinforce country ownership.

- Support only policies and programs for which the Bank has some clear evidence of ownership within the country (i.e., through the adoption of a PRSP in a participatory process)
- Potential for country ownership should be assessed through political economy analysis
- For Bank policy dialogue, rely on tailored policy analysis by government, Bank, or third parties rather than policy prescriptions
- Help strengthen recipient country’s capacity for exercising leadership
2. Agree up-front on a coordinated framework to evaluate performance under the program.

- Reach mutual understanding with the government and other donors on a single and internally coherent performance assessment framework for the government’s overall program, comprising policy and institutional actions, outputs, and outcome indicators
- Agree on a division of labor with other donors and seek to reduce transaction costs
- Where appropriate, follow the lead of other donors in specific areas
3. Customize the accountability framework to country circumstances.

- Ensure that the accountability framework builds on and is fully consistent with the country’s expressed policy intentions (i.e., government program, PRSP priority action plan, sector programs, budget)
- Do not use the accountability framework as instrument to add policy actions beyond the country’s own intentions
- Customize the detail, size, and frequency of review of the framework to specific country circumstances (capacity, aid dependency, vulnerability, reform readiness)
- Align modalities and timing of support to country- and program-specific needs
4. Choose only actions critical for achieving results as conditions for disbursements

- Choose policy actions from the performance assessment framework that are critical for the achievement of key program objectives as condition for disbursement or indicative prior action ("trigger") for future financial support
- Align conditions with CAS results framework
- Base conditions preferably on actions already taken rather than promised future actions
- Monitor output and outcome indicators closely, but be cautious in using them as annual disbursement conditions or triggers
5. Agree on a transparent review cycle conducive to predictable and performance-based financial support

- Review performance under the program in line with the country’s own M&E cycles (budget, PRSP review)
- Harmonize performance reviews with other donors and minimize transaction costs for the government
- Rely on and strengthen the country’s own accountability frameworks (parliaments), reporting systems, and arrangements for monitoring results
- Based on the Bank’s evaluation of performance, modulate the volume of financial support with a gradual response
- Announce financial support volumes early enough to be taken into account in making budget allocation choices for the next fiscal year
Next Steps
Next Steps

- **Fall 2005**: Dissemination of Review Findings
- **Fall 2005**: Implementation of Good Practice Principles
- **FY07**: Stocktaking of Development Policy Lending
Annex
Supporting Work Program
## External Consultations I

<table>
<thead>
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<th>Location</th>
<th>Host</th>
<th>Objective</th>
<th>Participants</th>
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<tbody>
<tr>
<td>December 2004</td>
<td>London Roundtable</td>
<td>UK (DFID)</td>
<td>Feedback on concept of review</td>
<td>Donors, academics, aid agencies, and civil society organizations</td>
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<tr>
<td>January 2005</td>
<td>London LICUS conference</td>
<td>ODI</td>
<td>Discuss conditionality in fragile states</td>
<td>Recipient governments, academics, donors, and NGOs</td>
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<tr>
<td>February 2005</td>
<td>Video-conference</td>
<td>World Bank</td>
<td>Discuss practice of conditionality with MDBs</td>
<td>Multilateral development banks</td>
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<td>February 2005</td>
<td>Paris</td>
<td>World Bank</td>
<td>Consultation with CSOs</td>
<td>International CSOs</td>
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<tr>
<td>April 2005</td>
<td>Berlin</td>
<td>Germany (BMZ/InWent)</td>
<td>Consultation with selected borrowers and donors</td>
<td>Borrowing countries, NGOs from those countries, and aid agencies</td>
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# External Consultations II

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<tbody>
<tr>
<td>April 2005</td>
<td>Washington</td>
<td>World Bank Spring Meetings</td>
<td>Consultation with LICs</td>
<td>Governments and parliamentarians of LICs</td>
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<tr>
<td>April 2005</td>
<td>Washington</td>
<td>World Bank Spring Meetings</td>
<td>Consultation with CSOs</td>
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<td>May 2005</td>
<td>Cape Town</td>
<td>World Bank/SPA</td>
<td>Exchanges on best practices in budget support</td>
<td>PRSP borrowing countries, academics, and aid agencies</td>
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<tr>
<td>June 2005</td>
<td>Washington</td>
<td>World Bank</td>
<td>Consultation with MICs</td>
<td>Governments of MICs, MDBs</td>
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# Additional External Consultations

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<th>Participants</th>
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<tbody>
<tr>
<td>January to June 2005</td>
<td>World Bank External Website</td>
<td>Open Consultation</td>
<td>Create an open forum for the review</td>
<td>General public</td>
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<td>May 2005</td>
<td>Internet</td>
<td>Independent Survey Consultancy</td>
<td>Survey of country authorities’ views on conditionality</td>
<td>High-level government officials from countries that have had policy-based loans FY00-05</td>
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## Analytic Work

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<tr>
<th>Contribution</th>
<th>Principal author</th>
<th>Objective</th>
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<tbody>
<tr>
<td>Issues Paper</td>
<td>OPCCE</td>
<td>Set out concept of conditionality review</td>
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<td>PRSC Retrospective</td>
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<td>Review experience with PRSCs</td>
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<td>Conditionality in Fragile States</td>
<td>OPCCE-LICUS</td>
<td>Good practice on development policy operations in LICUS countries</td>
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<td>Budget Support Groups and Joint Financing Arrangements</td>
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<td>Good practice note on operating principles of budget support groups</td>
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<td>Results in Development Policy Lending</td>
<td>OPCCE</td>
<td>Good practice in achieving a results-orientation in DPL</td>
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<td>OPCCE</td>
<td>Compilation of articles on conditionality</td>
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<thead>
<tr>
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<th>Objective</th>
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<tr>
<td>Summary of Consultations</td>
<td>OPCCE</td>
<td>Including LICUS, selected borrowers, LICs, and MICs</td>
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<td>Content of Conditionality</td>
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<td>Summary findings of survey sent to authorities of borrowing countries</td>
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<td>Subnational DPL</td>
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## Analytic Work

<table>
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<th>Trends in Policy-based Lending</th>
<th>OPCCE</th>
<th>Update of trends in numbers and content of conditionality, including aggregate Bank-Fund conditionality</th>
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<tr>
<td>Modalities of Bank Conditionality</td>
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<td>What, why, and how of conditionality Principal forms of conditionality (conditions, prior actions, triggers, difference from CAS triggers, etc.).</td>
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<td>Conditionality Review Paper</td>
<td>OPCCE</td>
<td>Conclusions of conditionality review and good practice principles</td>
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<td>Poverty and Social Impact Analysis (within the PRS Progress Report)</td>
<td>PREM</td>
<td>Status of PSIA work. Linkages between PSIA and policy-based lending</td>
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