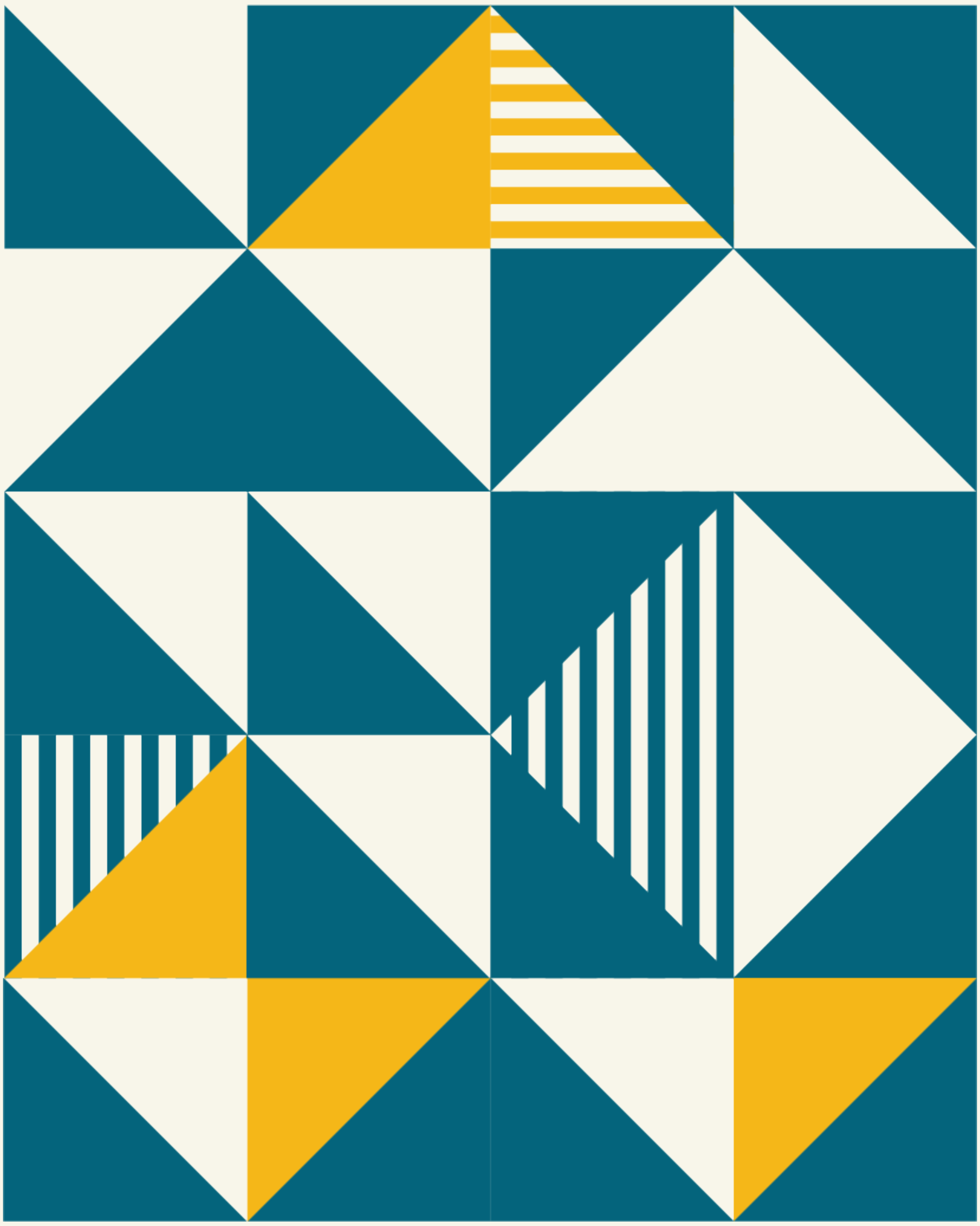
RENEWING THE MULTILATERAL DEVELOPMENT BANKS

FRANCISCO SAGASTI



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"The countries in a position to lend assistance … must provide [to] all the belligerent countries of continental Europe, allied and ex-enemy alike… a fund of $1,000,000,000 … [which] should be lent and borrowed with the unequivocal intention of its being repaid in full, [ranking] both for payment of interest and capital, in front of all Government indebtedness.… Expenditure out of the loan should be subject to general, but not detailed, supervision by the lending countries.… A guarantee fund [could be] established up to an equal amount (of which it would probably prove necessary to find only a part in cash), to which all members of the League of Nations would contribute according to their means." [2]

Lord Keynes, 1919

THE EMERGENCE OF THE MULTILATERAL DEVELOPMENT BANKS

My involvement with the Multilateral Development Banks (MDBs) began in the mid-1960s, when I became the student representative in the unit that managed an Inter-American Development Bank (IDB) loan to the National Engineering University in Lima, Peru. A few years later, as a graduate student, I was a member of the Wharton School team that advised the IDB on its use of computer technology. Notwithstanding this early start, I began to fully understand the genesis and functioning of the MDBs only years later, after reading John Maynard Keynes's *The Economic Consequences of Peace*.[3]

When World War I ended, the Allies imposed large financial reparations on Germany, which was hardly in a condition to pay. Keynes's prescient advice to avoid placing an excessive burden on the defeated countries was ignored at the Paris Conference and in the Versailles Treaty. He had proposed to assist Germany's economic recovery through loans and loan guarantees, but the victors were in no mood for concessions. Twenty-five years and another World War later, Keynes would get an opportunity to put his idea into practice in Bretton Woods, New Hampshire, where international negotiators gathered in 1944 to design the International Bank for Reconstruction and Development, now part of the World Bank Group.[4] His ideas also informed the design and implementation of the Marshall Plan for European reconstruction.

The main features of what are now known as the MDBs were anticipated by Keynes: lending institutions owned by and lending to countries, enjoying preferred creditor status, demanding full loan repayment, providing supervision and technical assistance to sovereign country borrowers and making a distinction between authorized and paid-in capital.

The International Bank for Reconstruction and Development focused initially on gaining the confidence of international capital markets and obtaining the highest possible credit ratings to issue bonds at low interest rates. This allowed it to raise funds for helping European countries recover from World War II. As its initial clients rebuilt their shattered economies, the World Bank shifted to support middle- and low-income countries without access to international capital markets at rates that would make it sensible for them to borrow by issuing bonds and other debt instruments.

The International Bank for Reconstruction and Development, and all the other MDBs that followed, are capitalized by member countries, with shares and voting rights allocated in proportion to capital contributions.[5] As envisaged by Keynes, they commit themselves to provide the full amount allocated to them (authorized or callable capital) only in exceptional conditions. However, MDBs shareholders are required to deliver a portion of their allocated capital contribution in cash (paid-in capital) which, together with retained earnings, constitute MDB equity.[6] Resources obtained through bond placements are loaned to member countries with a mark-up to cover operational costs. Even with this additional charge, interest rates are usually lower, and the period of repayment longer, than what most borrowers could get in global capital markets. The World Bank also provides concessional loans to low-income borrowers through the International Development Association, using funds obtained from replenishments from donor countries, and lends to private corporations through the International Finance Corporation, mobilizing resources by placing debt instruments in international capital markets.[7]

The International Bank for Reconstruction and Development's Articles of Agreement indicate that, "The total amount outstanding of guarantees, participations in loans and direct loans made by the bank shall not be increased at any time, if by such increase the total would exceed one hundred percent of the unimpaired subscribed capital, reserves, and surplus of the bank."[8] This provision implies that it, and the other MDBs that adopted a similar approach, have an exceedingly conservative one-to-one (authorized) capital to outstanding loans ratio. In comparison, under the international Basel III standards, the minimum capital adequacy ratio for commercial banks must be at least 10.5 percent of its risk-weighted assets.[9] Together with their preferred creditor status – which means MDBs are the first to be repaid when a borrower is in financial distress – few overdue repayments, and conservative loan/equity ratios, bonds issued by the World Bank and other MDBs are high-quality, low-risk investments.[10]

"Capital increases are important for the MDBs; otherwise, when total outstanding loans reach the authorized capital plus reserves, they will be constrained to lending only the reflows, or payments received from borrowers."

This is why capital increases are important for the MDBs; otherwise, when total outstanding loans reach the authorized capital plus reserves, they will be constrained to lending only the reflows, or payments received from borrowers. This constraint is considered by some World Bank member countries as too binding; at the 107th meeting of the bank's Development Committee, in April 2023, governments "agreed to consider a proposal to remove the Statutory Lending Limit (SLL) from the Articles of Agreement," based on a report from bank staff.[11]

By the early 2000s, the financing model envisaged by Keynes more than a century ago had spawned more than 30 MDBs in all the world's regions.[12] Their charters are remarkably similar, a testimony to the enduring relevance of the main features of these development finance institutions. Yet, as several experts on the capital adequacy of the MDBs have pointed out, in addition to capital increases, there is a need for these institutions to enhance their financing model by adapting their approach to risk tolerance, giving more credit to callable capital, expanding financial innovations, improving the ways in which credit rating agencies assess the financial strength of MDBs, and increasing access to MDB data and analysis.[13]

A CHANGED GLOBAL CONTEXT

New challenges and an increasingly turbulent world demand a major rethinking of international collective action schemes, particularly the MDBs. Climate change, biodiversity loss, water scarcity, science and technology disparities, international and civil wars, migration, pandemics, and transnational organized crime have been added to the list of issues that require supranational efforts and joint initiatives.

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The last few years and months have seen several proposals to reform and revitalize the international financial institutions to address global challenges. For example, calls to update their missions, increase their capacity to mobilize financing, reform conditions for access to loans, and update the way they operate have been recently made by a group of independent think tank leaders.[14] In addition, drawing on the *2022*

Bridgetown Agenda for Reform of the Global Financial Architecture, Mia Mottley, the prime minister of Barbados, and Rajiv Shah, president of the Rockefeller Foundation, have highlighted "the urgent need to update institutions built for a different era."[15] The United Nations has put forward proposals to reform the international financial architecture, focusing on global economic governance, debt relief, and policy and regulatory frameworks, among other issues.[16]

Proposals to reform the World Bank were included in a report to the bank's governors at the April 2023 Development Committee meeting.[17] That report includes proposals to enhance its mission, strengthen operations, and adapt its financial model. It recognizes that developing countries face three sets of global challenges: climate change, pandemics and health security, and fragility and conflict. These proposals have met with mixed reviews, and some observers argue there is a need for more radical approaches.[18]

Under the proposed reforms, beyond the elimination of extreme poverty and achieving shared prosperity, the World Bank mission would include fostering "sustainable, resilient and inclusive development." Its operational model would evolve towards a broader approach to country programming; promote strategic regional and global partnerships; improve its crisis response capabilities; facilitate the flow of private capital; and better mobilize domestic resources. Adjustments in the World Bank financing model would build on its track record of balance sheet optimization, protecting its triple-A rating and maintaining its preferred creditor status. An important addition to its operational and financial model would be an expanded effort to provide international and global public goods.[19]

Regional and subregional multilateral development banks often take a cue from the World Bank, and most are following, to varying degrees, similar approaches. However, two recently created MDBs – the Asian Infrastructure Investment Bank and the New Development Bank[20] – have expressed a willingness to differentiate their mission and activities. Yet, global challenges make it likely they will adjust their strategies roughly in the same direction as that of the World Bank. Moreover, it is necessary that MDBs function much more as a system, rather than as a somewhat disconnected group of development finance institutions (See Box 1).

BOX 1: THE MULTILATERAL DEVELOPMENT BANKS AS A SYSTEM

Each multilateral development bank has a different set of constituencies to which it is accountable and must develop a strategy to respond to what has become a rather complex set of disparate and conflicting demands. However, what may be described as *the different "personalities" of the MDBs should not prevent visualizing them in an integral manner, as a set of organizations that share common characteristics, play similar roles and conform broadly to the same institutional model.* Considered as a whole, they constitute a[n] [80-year-old] institutional innovation to channel financial resources and knowledge from richer to poorer countries, while at the same time providing a range of complementary services to its various constituencies.

If stakeholders are to adopt a systemic approach to the MDBs, a major shift in perspective will be required. This would move beyond the current practice of focusing on the World Bank, and occasionally on one or another regional development bank, and would try to establish a broad strategic framework aimed at making the entire system function better. Such an approach would necessarily include the subregional MDBs and other funds that operate similarly to the MDBs. Viewed in this perspective, the challenge is to transform a set of disparate institutions into a more efficient network and eventually into an effective system. This has important implications for the division of labor between MDBs and for the coordination of their activities in their borrowing countries. Yet, this should not entail the elimination of unique qualities, experiences, and comparative advantages. The World Bank and a smaller subregional bank should not be expected to function in identical ways. Differences and distinct personalities should also be respected and even encouraged, and the aim should be to achieve a balance between unity and diversity in the system.

Far from functioning as an integrated system, however, it must be said that the MDBs currently behave more like a dysfunctional family, primarily in the field. Relations between the World Bank and the regional development banks are strained in several regions and in many countries, while most subregional MDBs have little interaction with the World Bank. Differences in management styles, extent of field presence, relations with borrowers, technical competence, knowledge of the region and countries, among others, combine to create sources of tension that could and should be reduced by taking a more systemic approach to the operations of MDBs.

Source: Institute for Development Studies, *A Foresight and Policy Study of the Multilateral Development Banks.*

THE ROAD AHEAD

Proposals to update and enhance the functioning of the MDBs have largely been made from what could be seen as a "supply-side" perspective of what these institutions are doing or should do. A "demand-side" point of view would be complementary. From a client's viewpoint, MDBs do more than mobilize and channel financing. These institutions also provide a range of services that include policy advice, capacity building, technical assistance, and institutional support. In addition, they arrange and finance the provision of global and international public goods.

Financing

Raising, providing, and intermediating development finance is the key activity of the MDBs. These institutions now have at their disposal larger amounts to lend and a broader range of financial instruments – soft, blended and regular loans, guarantees, trust funds, equity investments, donations, among others. Yet, there is agreement that the financing capacity of MDBs should be significantly expanded through capital increases, shareholder guarantees, further balance sheet optimization measures, and additional grantmaking resources, among other measures. While the World Bank and other MDBs still have headroom before hitting their statutory lending limit, prudential rules and rating agencies are focusing their attention more closely on their equity to loan ratios, which remain robust.[21]

"Careful attention should also be paid to calls for de-risking private sector investments; it will be important to incentivize private flows without guaranteeing corporate profits."

Borrowing countries access to different types of loans and conditions are mostly determined by their level of development, usually proxied primarily through income per capita indicators. Although applied in a flexible manner, this indicator does not appear adequate in the highly diversified development scene of the 2020s. The World Bank and other MDBs have begun to tailor loans and other financial instruments to the needs of a more varied set of countries but should move more aggressively in this direction.[22] Measures to promote and leverage private sector financing are also crucial but require aligning profit-making motivations with the needs of middle- and low-income countries. This is not always an easy task, as social and environmental conflicts have often accompanied private infrastructure and extractive industries investments.[23] Careful attention should also be paid to calls for de-risking private sector investments; it will be important to incentivize private flows without guaranteeing corporate profits.

The critical level of foreign indebtedness of many low- and middle-income countries calls for urgent debt relief schemes similar, but much more audacious, to those of the 1980s and 1990s.[24] While MDB debt does not account for a high share of external liabilities for many of these countries (except for some low-income ones), they can and should play a leading role in debt cancellation, reduction, and debt swap schemes with all creditors, including China, the largest loan provider to many low-income countries in Africa and Asia.[25] The objective would be to put these countries on a better financial standing to confront development challenges and especially those – like climate change and geopolitical disruptions – for which they bear little responsibility and over which they have little control.

Furthermore, most MDB borrowers have been public sector institutions in individual countries, in part because of the need to ensure timely repayments. Yet, new development challenges transcend national borders and require joint country efforts. Notwithstanding the considerable difficulties of loan servicing and burden sharing among several sovereign borrowers, it is necessary to design and implement multi-country financial schemes, particularly for the provision of global and international public goods. The International Development Association, in the World Bank Group, has a regional window to support multi-country initiatives in Africa through concessional loans and grants, but its operations are limited, and bolder approaches are required.[26]

Additional and Complementary Services

MDBs now face the reality that many of their traditional middle- and upper-middle-income borrowers can tap international capital markets on similar or better terms than MDB loans.[27] Countries that have direct access to international bond markets on favorable terms continue to borrow from the MDBs, largely because the additional services they provide offset higher borrowing costs. Beyond taking measures to ensure repayment, international capital markets place no conditions on countries that issue sovereign debt, but neither do they provide the complementary services offered by MDBs, such as policy advice, capacity building, technical assistance and training, networking with public institutions in other countries, and legal protection against the possible misuse of funds.

Policy advice has been a useful, though often controversial, staple of the MDBs. Standardized policy advice and recommendations, as well as conditions imposed on countries with little government buy-in and limited chance of sustainability, have become less common than in the past. But they could be further adjusted to better fit country situations. Frequently bound with cross-conditionality with International Monetary Fund (IMF) programs, World Bank policy conditions often impose policy constraints on development efforts. Abandoning or moderating IMF cross-conditionality would not mean giving up assurances that loans would be adequately employed and repaid but would allow greater flexibility to tailor policy recommendations to specific circumstances and capabilities. It would also neutralize the potentially negative impact of IMF-World Bank cross-conditionality and of IMF macroeconomic policy prescriptions, which often implicitly embed constraints that distort domestic social and environmental policies.

Capacity building, technical assistance and institutional support programs have been a regular feature of MDB operations, mostly associated with loans, but also in stand-alone engagements. They have helped to strengthen public sector capabilities and assist in the effective use of external financing and mobilization of domestic resources, frequently by supporting local think tanks that conduct policy-oriented research and by training public sector officials. MDBs also have fostered cooperative arrangements between their borrowers, facilitating the horizontal transfer of experiences and expertise. In addition, the legal status of their loan contracts can protect public sector institutions managing MDB funds from undue political interference.[28]

The range of complementary services and support activities provided by the MDBs could be expanded and upgraded through far-reaching partnerships with international civil society organizations and academic institutions. Policy advice, capacity building, technical assistance, institutional support and training programs could also benefit from intensified cooperation between borrowers and among borrowers and industrialized countries.

Global and International Public Goods

The provision of global and international public goods has become critical, as challenges that demand supranational action have increased in recent decades. This requires far more emphasis by MDBs in collaboration with other international institutions and agencies. Arrangements for global and international public goods provision and financing are a matter of negotiation at the international level, but those who produce and benefit from these public goods are ultimately found in a multiplicity of local settings. Therefore, high-level political agreements to provide and finance global and international public goods must be accompanied by the design and implementation of multilevel delivery systems, decisions on institutional divisions of labor, and the exploration of financing options for their core and complementary components. This is the only way of ensuring they benefit their producers and users at the local level.[29]

The growing challenges of a more closely interconnected and unstable world require a major ratcheting-up effort to collectively address them through the provision of global and international public goods. Climate change adaptation and mitigation, protecting biodiversity and conserving ecosystems, controlling the spread of disease and improving health care, reducing pollution, maintaining peace and security, preserving global economic and financial stability, and creating global standards and information sharing arrangements all demand joint international efforts. Emphasis should be placed on cooperative initiatives to build science, technology, and innovation capacities in middle- and low-income countries, a necessary condition for them to help meet the growing range of global challenges. Disparities in the capacities to generate and utilize scientific and technological knowledge dwarf almost any other indicator of inequalities between industrialized and developing countries, which hampers the capacity of poorer countries to adequately engage in the provision of global and international public goods.[30]

"MDBs have the combined reach, clout, and financial muscle to provide global and international public goods at the scale required to begin addressing supranational challenges."

The World Bank, Inter-American Development Bank, and Asian Development Bank have created programs to provide global and international public goods, largely financed by trust funds and allocations from their net income.[31] MDBs have the combined reach, clout, and financial muscle to provide global and international public goods at the scale required to begin addressing supranational challenges. They should do so urgently, in concert with United Nations organizations; the secretariats of the various conventions and special funds that focus on public goods; private foundations and civil society organizations at the international and regional levels; private firms engaged in environmental, social, and governance (ESG) initiatives; and local communities. These efforts should lead to the design and implementation of delivery systems tailored to specific global and international public good, ensuring that policies and resources support the local production and broader consumption of public goods.

AN AGENDA FOR RENEWAL

There is growing recognition of the multiple transnational dangers that threaten hard won – but highly uneven – global gains in the quality of life, and this recognition has begun to prompt calls to action. Against this background, it is natural to focus on the role of MDBs, the most successful institutional innovation to mobilize development finance.

First, considering the vast amounts of financial resources that will be required to address global challenges, it is essential to ensure that MDBs have the necessary capital and financial tools to support country initiatives and the provision of global and international public goods. This should start with a joint review of the capital adequacy frameworks of MDBs and continue with an assessment of a wide variety of financial instruments, examining the amounts they could mobilize from different sources. Taking into consideration the vastly changed geopolitical context of the 2020s, MDBs should work with the United Nations[32] and other international agencies, civil society organizations, local community representatives, foundations, private sector associations, and academic institutions from developing and developed countries to evaluate the fitness and effectiveness of international development cooperation schemes.

Second, regional MDBs are now facing urgent reconstruction tasks in war-torn countries. In a curious historical twist, harkening back to the initial motivation for creating the International Bank for Reconstruction and Development after World War II, both the European Bank for Reconstruction and Development and the European Investment Bank are allocating billions of euros to the reconstruction of Ukraine's infrastructure, even while hostilities are raging.[33] Estimates made by a group of international organizations and the World Bank in mid-2022 put the cost of reconstruction in Ukraine at $411 billion. A recent Islamic Development Bank report indicated that about $88 billion would be required to repair losses from the violent conflicts in the Middle East.[34] In 2021, the Asian

Development Bank adopted new flexible processes and procedures to tailor interventions to the challenges of fragile and conflict-affected situations and small island developing states.[35] The African Development Bank defined in 2022 a strategy for addressing fragility and building resilience in the region, acknowledging that violent conflicts placed several African countries in a precarious situation.[36]

A complex balancing act will be required by the World Bank and regional MDBs to respond to the demands of climate change, pandemics, inequalities and poverty, while also engaging in long-term and costly reconstruction interventions in war-torn countries. It is possible to address both sets of challenges simultaneously, but this requires not only the financial and technical expertise of MDB staff, but also conflict resolution skills and political talent that have been associated more with other international organizations.

Third, there is a need for MDBs to expand and upgrade their complementary services, particularly by supporting policy research in the countries they work with. In addition to the research and training activities conducted in-house at MDBs, such as those of the World Bank Institute and their counterparts in regional development banks, it may be useful to review and build upon initiatives to support independent think tanks in developing countries, and to enhance the foresight capabilities of government agencies and other organizations in the private sector and civil society.[37]

As the global context for economic, social, and geopolitical development has changed, and continues to evolve, it will be necessary for MDBs to rethink and adjust their policy recommendations. Among many others, one sign of the willingness of major powers to modify the policy consensus of past decades – especially regarding the roles played by markets and the private sector on the one hand, and governments and regulatory agencies on the other – were the recent statements by the U.S. national security adviser and the president of the Federal Reserve. They anticipate a larger role for industrial policy and government interventions in guiding economic policy, which could influence the nature of the advice provided by the World Bank, the IMF, and regional and subregional MDBs.[38]

Fourth, considering the magnitude of the knowledge divide between rich and poor countries, it is imperative to design and put in place collaborative schemes at the regional and global levels to create and consolidate scientific research, technological development, and innovation capabilities in developing countries. This may require the creation of science, technology, and innovation financing facilities at the regional and global levels in fields of common interest, a task for which triangular cooperation schemes between developing and industrialized countries are particularly well suited. Scholarly and private sector organizations could participate in such schemes, aimed at bridging the knowledge divide in areas that are critical for national development and for meeting global challenges.[39]

Fifth, in taking seriously the provision and financing of international and global public goods, it will be imperative to transcend the high-level discussions that center around who should pay, how much and for what. Instead, it is necessary to focus on designing delivery systems that connect high-level international political decisions with the local actors that generate and utilize the public goods in specific settings. For each global or international public good that political leaders reach a consensus on the need to provide and finance, it crucial to involve the broad range of actors that play leading and supporting roles in the delivery of those public goods. (See annex.)

Finally, during the last eight decades, MDBs have evolved into a group comprising more than 30 organizations that include global, regional, and subregional MDBs, and special funds that mimic some of their features. As Box 1 suggests, they should now work as a system with greater coordination, a more deliberate division of labor, and a determined push towards renewing their mandates and operations. The recently appointed presidents of the two oldest MDBs, Ajay Banga at the World Bank and Ilan Goldfajn at the IDB, should take the initiative in convening the heads of all other MDBs and related institutions to identify measures that could create a more effective system of sustainable and equitable development finance institutions.

Both leaders bring unique perspectives to their new roles. Banga was born and educated in India. He achieved success in the United States and international business world, leading an international private bank with thousands of employees that works all over the world. Born in Israel, Goldfajn was raised and educated in Brazil, earned his academic credentials in the United States, and was an outstanding central banker before joining the IMF to lead its Western Hemisphere division. Both have strong support from member countries in their institutions, as well as from a variety of stakeholders in the public, private, civil society, and academic sectors. They could jointly exercise political leadership and a key role in the evolution of MDBs towards a more effective system of international development finance institutions.

CONCLUDING REMARKS

We should remember that Keynes's advice was not heeded after World War I. He had to wait 25 years and witness the tragedies of World War II before his ideas were to materialize with the creation of the International Bank for Reconstruction and Development, which provided the model for many other MDBs, the most successful development finance innovation of the last century. As part of a broader agenda of reforms to the international financial architecture, we must not wait for a World War III, a climate catastrophe, another deadly pandemic, or some other devastation to renew and empower the MDBs for the monumental tasks at hand.

ANNEX:
ARRANGING FOR THE PROVISION AND FINANCING GLOBAL AND INTERNATIONAL PUBLIC GOODS

Note: *This annex is a slightly edited excerpt from the executive summary of Francisco Sagasti and Keith Bezanson's book, "Financing and Providing Global Public Goods: Expectations and Prospects," published by the Ministry for Foreign Affairs of Sweden in 2001 (available at https://eba.se/wp-content/uploads/2021/04/2001.2-Financing-and-Providing-Global-Public-Goods-Expectations-and-Prospects.pdf). The book contains a review of the literature through the date of publication, a fully developed conceptual framework, and five case studies on the application of the delivery system summarized in this excerpt.*

INTRODUCTION

The confusion and ambiguities that have become evident in discussions linking global public goods and development cooperation indicate the need for greater clarity and an agreed conceptual framework. If this is to be achieved, a first question is to define what exactly is a global public good, before determining how to provide it. The theory of public goods offers only very limited assistance in arriving at meaningful definitions that are also useful for policy choices. Second, the collective action problems that are inherent to public goods in general apply to global and international public goods to a larger extent. Even if there is general agreement that the potential gains from international concerted action are great, there are no supranational government bodies with the power and authority to straightforwardly devise and impose measures equivalent to those at national level (e.g., taxation, regulation, market creation) that would lead to the provision of public goods.

In the third place, the range of spillovers across countries can vary significantly. This begs the question of how international a public good must be before being considered as a global public good. It is obvious that the broader the range of spillovers the more global a public good would be. But the boundaries between international and global public goods are quite diffuse and these terms are frequently used interchangeably. Finally, regardless of how global or international a particular public good is, it must ultimately be generated and utilized by individuals or agents at specific locations. For this reason, for the existence and provision of an international or global public good it is necessary to differentiate between the *core component* of the delivery system, which should be taken care of by the international community, from the *complementary component* of activities that are the primary responsibility of national and local entities.

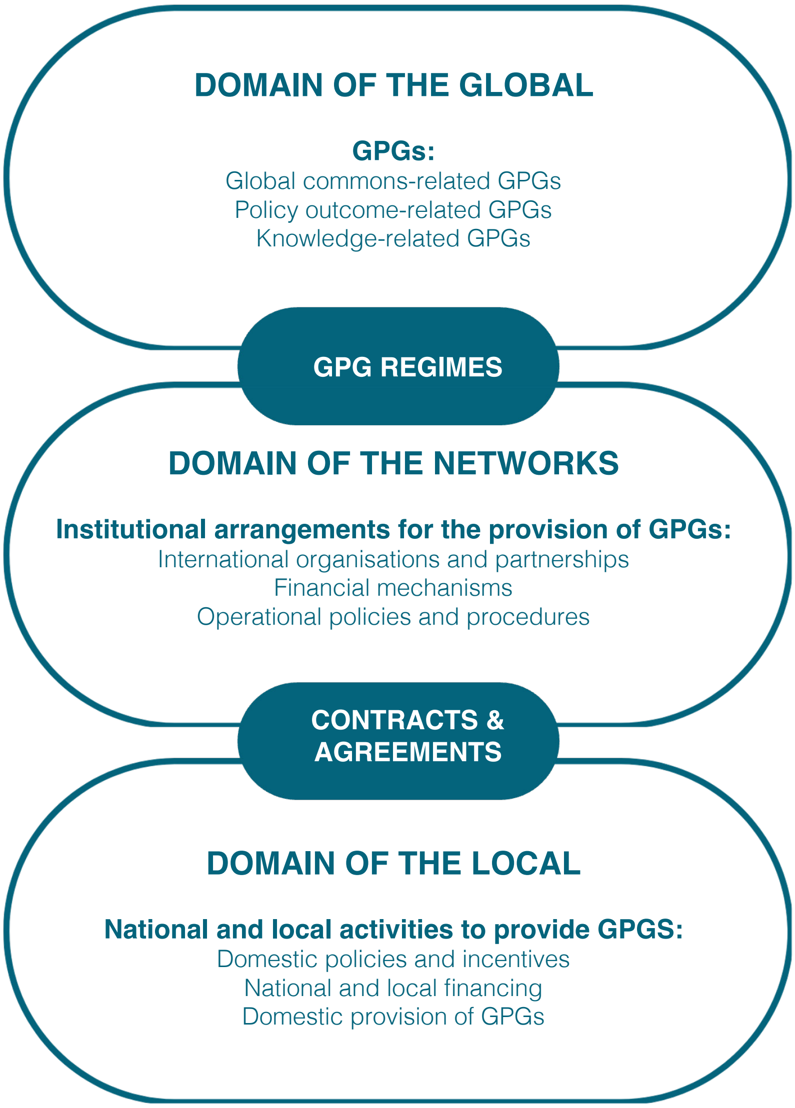
Consequently, the transition from acknowledging a good, service or outcome as desirable to declaring that it is a global or international public good is anything but straightforward or automatic. It is heavily influenced by public awareness, political decisions and requires collective action at the level of the international community, which includes not only national governments, but also private corporations, civil society organizations and academic institutions. It also begs the question of desirable for whom? Declaring something to be a global or international public goods has meaning only when embedded in a political process that leads to measures that ensure its delivery.

AN INTERNATIONAL PUBLIC GOODS DELIVERY SYSTEM

One way to conceptualize the requirements outlined in the foregoing section and to integrate the various issues that have been raised in discussions about global public goods, is to articulate what may be defined as an idealized international public goods delivery system. Such an idealized construct can help to separate the elements that constitute the core component of a global public good delivery system in a more restricted sense from those that relate to the complementary regional, national and local activities involved in its production, delivery and consumption, placing all of them in a common framework.

The components of an idealized international public goods delivery system can be placed in the three domains of the fractured global order.[40] As shown in Figure 1, the process of agreeing on what constitute global public goods— whether related to the global commons, to global policy outcomes or global knowledge— belongs in the domain of the global. The host of institutional arrangements, including international organizations and partnerships, supranational financial mechanisms, and operational policies and procedures that oversee ensuring that the global public good is made available belong in the domain of the networks. The multiplicity of national and local activities related to the actual production and consumption of global public goods, which include domestic policies and incentives, national and local financial mechanisms, and the activities of government agencies, private firms, civil society organizations and individuals, belong in the domain of the local. The conventions, treaties and protocols that formalize agreements for the provision of a global public good —also known as global public good regimes— mediate between the upper two domains. Contracts, agreements and other lower-level legal instruments mediate between the lower two domains.

FIGURE 1: THE THREE DOMAINS OF GLOBAL PUBLIC GOODS



It follows from this conceptualization of an idealized system that attempts to define and arrange for the provision of global public goods cannot avoid issues of asymmetrical knowledge, capacities to benefit, differences in values and power relationships. It follows equally that any claim that something is a global public good is merely exhortation, unless the essential elements to deal with these issues, that is, the delivery system, have been established. Seven such elements are suggested and are summarized in Figure 2. These are:

1. ***Knowledge, public awareness and political decisions.*** Declaring that something is a global public good depends primarily on knowledge about its characteristics and effects, the extent of public awareness and pressures to provide the global public good, and on the political decision that providing the global public good merits concerted actions by the international community.

2. ***Global public goods regimes.*** Regimes are a key concept in the literature on international relations with obvious application to global public goods. Regimes have been defined as the "arrangements peculiar to substantive issue-areas in international relations that are characterized by the condition of complex interdependence." The regimes in an idealized international public goods delivery system would include the conventions, treaties, protocols, agreements and other legal instruments resulting from negotiations in an issue-area. However, not all regimes require complex intergovernmental negotiations and may be a result of the gradual evolution of practices, implicit agreements and ad-hoc arrangements between the various parties involved in a particular issue-area. The nature of the interactions between the parties interested in its provision will influence the results of such negotiations.[41]

3. ***International organizations and partnerships.*** Intergovernmental organizations, specialized secretariats or partnerships between public, private and civil society organizations are required to interpret, administer, monitor, enforce and evaluate the provisions specified in the agreements that give rise to the global public goods regime.

4. ***Financing mechanisms.*** The provision of international and global public goods requires that special resources be allocated to finance the activities involved in their delivery. A whole host of activities, from raising public awareness and negotiating international public goods regimes, to the performance of specific tasks at the local level that provide the public good, need to be considered in the design of financial mechanisms. There is a major issue and considerable controversy over applying financial resources whose purpose is development assistance (i.e., ODA) to the provision of global and international public goods. It is highly questionable that ODA be applied for the purpose of providing public goods

that benefit developed countries at least as much as developing one. Additional resources are required, above and beyond ODA, for this purpose.

5. ***Operational policies and procedures.*** These refer to requirements for the consistent and effective application of the principles and norms of global public good regimes (i.e., the policies, decision-making procedures, regulations, codes and other rules internal to the organizations and financing mechanisms).

6. ***Agreements and contracts.*** Mediating between entities placed in the domains of the networks and of the local in an international public goods delivery system, are many types of lower-level legal instruments. These specify the terms of reference, obligations and rights of the national and local entities involved in the actual production and consumption of a global public good.

7. ***Capabilities and arrangements for the inclusion of national and local entities in the provision and consumption of a global public good.*** The last component of an international public goods delivery system refers to the government agencies, private firms, civil society organizations and individuals that are involved in activities that produce or consume a global public good at the local level.

An idealized international public goods delivery system would be made up of all the components indicated above, extending from the core component (the upper trapeze in Figure 2) to the complementary regional, national and local activities linked to the provision and consumption of the good (the lower trapeze in Figure 2). As Figure 2 suggests, the way in which these two sets of activities —the core and the complementary— relate to each other is perhaps the most crucial aspect in establishing arrangements for the provision of international public goods.

The main question is: how far to go down along the continuum from global to local activities in defining what constitutes the core element of the global public good delivery system? The answer to this question will, in turn, determine which international organizations and programs should be involved in their provision and, most importantly, how the provision of the global public good should be financed.

A decision could be made to clearly separate the core component from the complementary activities of the international public goods delivery system, and to limit the financing arrangements associated with the global public good just to the core component (for example, to produce and guarantee just the availability of HIV/AIDS drugs at a reasonable price). This would imply that regional, national and local entities would have to make their own preparations to finance and organize the complementary activities (purchase, storage, allocation, distribution, application in the case of HIV/AIDS drugs), although this would have to be done in close coordination with the entities in charge of the core component.

Alternatively, a decision may be made that the core component of the global public good should incorporate the organization and financing of the means to deliver it all the way down to the national and local levels (for example, to provide treatment for HIV/AIDS infected persons on the ground). In this case, the complementary activities in the delivery system would overlap with and, in effect, could be considered as part of the core component, and in consequence should be included in the financial arrangements associated with that component.

The conceptual framework for an idealized international public goods delivery system identifies the elements that must be in place for a global public good to be defined, generated and utilized. It invites and assessment of what is missing in the delivery system for a particular global or international public good, and of how far down should the core component go to ensure its provision. At the same time, it underscores the point that there is no way of avoiding values, interests and power relations in defining what is a global public good; that the knowledge of epistemic communities is critical to underpin a decision and to establish global public good regimes; that institutions and partnerships, financing mechanisms, and operational policies and procedures are required at the international level to facilitate the generation of the global public good; and that all of the preceding arrangements would be useless without the identification and involvement of national and local entities that will be in charge of actually producing and utilizing the global or international public good at the local level.

EXPLORING FINANCING OPTIONS FOR THE PROVISION OF GLOBAL PUBLIC GOODS

Even with all the problems of definition and of obtaining accurate figures, there is no doubt that increased resources have been allocated over the last decade of the twentieth century to what have become broadly considered as global public goods. The World Bank estimates that during the mid-1990s, approximately 30 percent of the $55 billions of total Official Development Assistance was allocated directly and indirectly to global public goods. The core component was estimated at about $5 billions with another $11 billions allocated to the complementary activities necessary to produce and consume the global public good. The Bank also draws attention to the fact that this is an allocation trend that appears to be increasing.

This trend has produced expressions of deep concern to the effect that this amounts to a net transfer of resources away from developing countries. For this reason and because of the multiplicity of channels that could be involved in an international public goods delivery system, a scheme for the systematic exploration of financing options is needed. Figure 3 suggests a framework to begin such exploration. It consists of a sequence of questions to guide examination of the range of financial mechanisms that have been used in practice or have been proposed. The framework applies primarily to the financing of the core component of a global public good, and to a lesser extent to the regional, national and local activities (complementary component) linked to the provision of the global public good.

As indicated by the dotted lines at each node in Figure 3 choices are not necessarily combinations to different degrees of the various branches are possible, which would lead to a mixture of financing mechanisms for a particular global or international public good. Partnerships between different types of institutions would usually lead to such combinations of financing mechanisms. They could involve intergovernmental agencies, private corporations, foundations, special funds, academic institutions, non-governmental organizations, national and local government agencies, among other entities, to ensure that decisions about the provision of global and international public goods is adequately financed.

FIGURE 2: AN INTERNATIONAL DELIVERY SYSTEM FOR GLOBAL PUBLIC GOODS

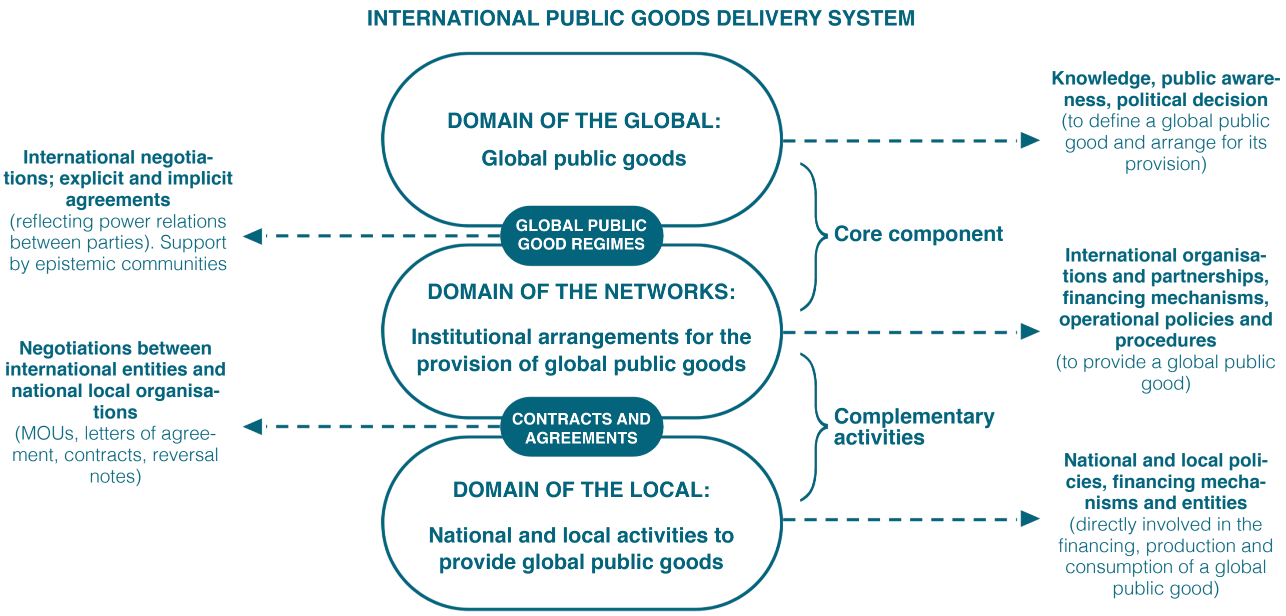
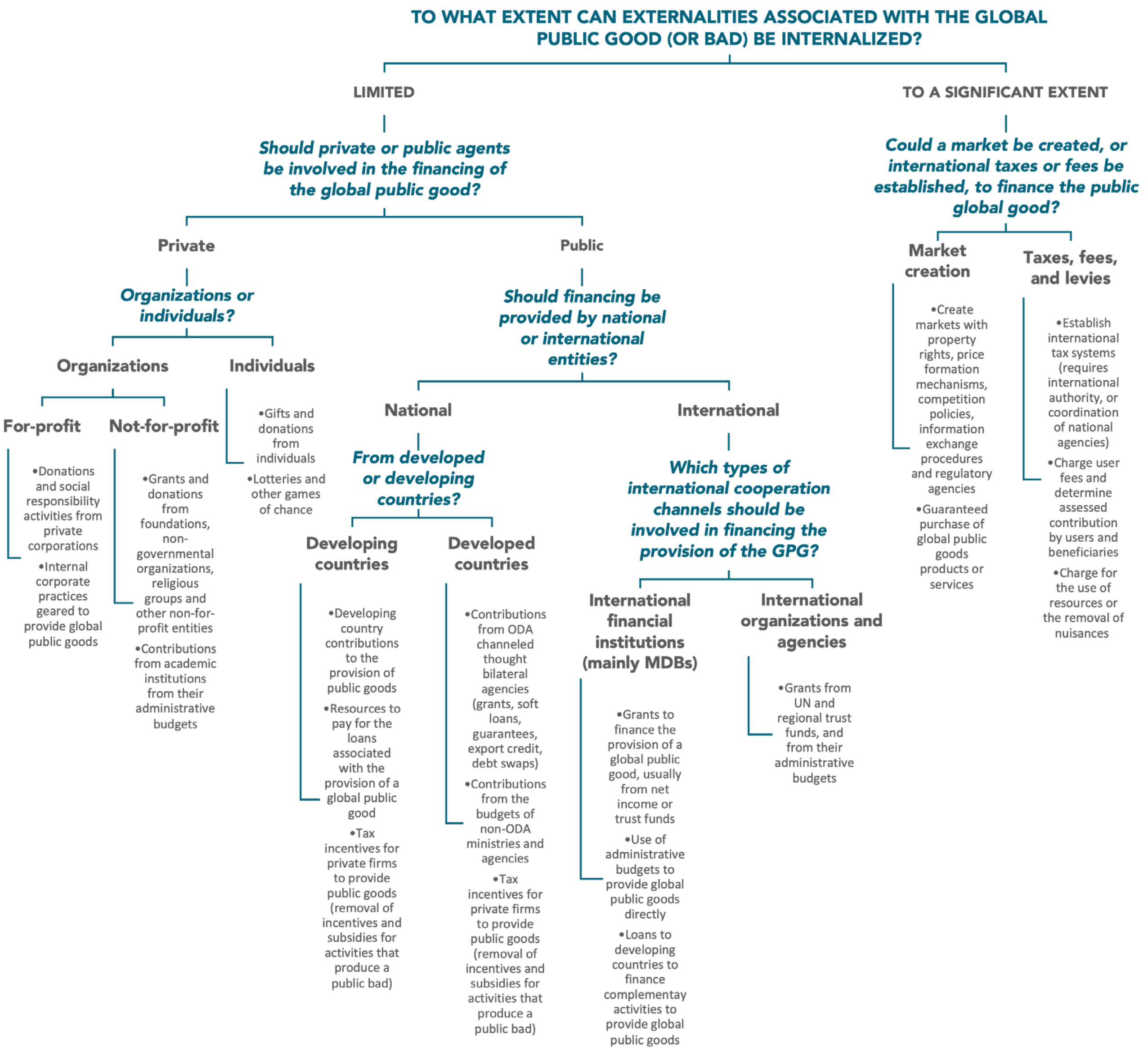


FIGURE 3: DECISION TREE TO EXPLORE GLOBAL PUBLIC GOODS FINANCING OPTIONS



Notes to Figure 3: (a) The framework to explore financing options applies mainly to financing of the core component of an international public good (less so to complementary activities) and the questions should be adapted to each specific global good and distinct case. (b) Choices are not necessarily ‘either-or’. Financing mechanisms could involve partnerships. Combinations of private and public financing may be required even in cases of market mechanisms, fees and taxes.

ENDNOTES

1 Former president of Peru; Fellow, Woodrow Wilson International Center for Scholars, Washington, DC; Professor, Universidad del Pacífico, and Senior Affiliated Researcher, Instituto de Estudios Peruanos, Lima, Peru.

2 Keynes, The Economic Consequences of the Peace.

3 Paraphrasing Joni Mitchell, "I have seen MDBs from both sides now"; I have been chief of the Strategic Planning Division of the World Bank and an adviser and consultant on MDB matters at several bilateral and multilateral organizations, as well as a member of the boards of executing units of MDB loans and an adviser to governments that received them. In addition, I dealt with MDB matters as a congressman and president of Peru. All of this has helped me understand the operating logics of both MDB staff and national government officials, and enhanced my appreciation of the key role that MDBs can and should play in addressing the pressing challenges humanity will face in the coming decades.

4 The World Bank Group now comprises the International Bank for Reconstruction and Development, which provides loans mostly to its middle-income borrowing member countries; the International Development Association, created in 1960 and financed with replenishments, which provides loans to low-income countries on more favorable terms; and the International Finance Corporation, created in 1956, which provides loans and equity investments to private corporations in member countries. It also includes the Multilateral Investment Guarantee Agency and the International Center for Settlement of Investment Disputes.

5 Its larger shareholders are the United States (15.79 percent of voting power), Japan (7.44 percent), China (5.33 percent), Germany (4.10 percent), and France and the United Kingdom (3.92 percent each).

6 As Moody's has observed, "In addition to retained earnings from its operations, the bank's capital position is further supported by periodic equity contributions from shareholders. On October 1, 2018, the shareholders approved a new capital increase package of $60.1 billion, comprised of $7.5 billion of paid-in capital and $52.6 billion of callable capital, which would be paid in over the next five years." (Bissessur, "Final Moody's Issuer In-Depth – IBRD.") For example, in the International Bank for Reconstruction and Development's last capital increase, in 2018, the paid-in portion amounted to about 12.5 percent. In addition, part of the retained net income of the MDBs has been used to increase the proportion of equity at their disposal and thus – in addition to its one-to-one loans/authorized capital ratio – to maintain a conservative equity/loans ratio of 22 percent in 2022 that further bolsters financial strength.

7 IFC issues debt instruments in international capital markets, leveraging its fully paid capital contributions from member countries and its retained earnings (International Finance Corporation, "Management's Discussion and Analysis").

8 World Bank, "IBRD Articles of Agreement III," Section 3.

9 Nickolas, "What is the Minimum Capital Adequacy under Basel III?"

10 As Clemence Landers and Rakan Aboneaaj have pointed out, "MDBs have strong underlying fundamentals underpinned by their preferred creditor status, backing from their shareholders (often partly in the form of callable capital), and uniquely low loan impairment rates (when principal and interest are not repaid in full). The [International Bank for Reconstruction and Development], for example, has a 0.2 percent nonaccrual rate (the percentage of loans over 89 days

overdue), a fraction of the nonaccrual rate for commercial loans in the United States, yet holds significantly more capital than private sector peers." (Landers and Aboneaaj, "Half a Trillion in Dry Powder?").

11 World Bank, "Chair's Statement: 107th Meeting of the Development Committee."

12 Sagasti and Prada, "Regional Development Banks."

13 See, for example: Independent Expert Panel, "Boosting MDBs' Investing Capacity," and Kharas and Bhattacharya, "The Trillion-Dollar Bank."

14 Center for Global Development, "Reforming the World Bank and MDBs."

15 Mottley and Shah, "How to Revitalize the World Bank, the IMF, and the Development Finance System"; Ministry of Foreign Affairs and Foreign Trade of Barbados, "The 2022 Bridgetown Initiative."

16 United Nations, "Out Common Policy Agenda Policy Brief 6: Reforms to the International Financial Architecture."

17 Development Committee, "Evolution of the World Bank Group."

18 See, for example, Charles et al., "What We Saw at the 2023 Spring Meetings."

19 Development Committee, "Evolution of the World Bank Group." This report charts the necessary steps to adjust the World Bank functions and activities to a vastly changed global context. Yet, it also highlights the continuity in its development efforts. A cursory glance at the Framework for Strategic Choices prepared at the end of the 1980s, when the developing countries' debt crisis, the beginning of the fall of the Soviet Union, and the emergence of environmental concerns coincided with a major reorganization of the World Bank, suggests the persistence of long-standing development concerns (World Bank, "A Framework for Strategic Choices").

20 The Asian Infrastructure Investment Bank began operations in 2016, with China as its largest shareholder. The New Development Bank was established in 2015 by the four BRICS countries (Brazil, India, Russia, and South Africa) as shareholders.

21 For a definition of 'headroom," see: Stern, "World Bank General Capital Increase," Pages 21-23.

22 Ferranti, "The World Bank and the Middle-Income Countries."; Sagasti, "From 'Graduation' to 'Gradation' in International Development Finance."

23 A recent report on how MDBs could mobilize private capital focuses on the various instruments MDBs have at their disposal to reduce risk for private investors, diversify investment opportunities, and lower transaction costs. It would be useful to complement analyses of this type with an assessment from the perspective of recipient countries (Gregory, "Taking Stock of MDB and DFI Innovations").

24 In 1996, the World Bank and International Monetary Fund launched the "Highly Indebted Poor Countries Initiative" to "ensure that no poor country faces an unmanageable debt burden," and created a trust fund with complementary bi-

lateral finance for providing 100 percent relief on eligible debts by these institutions (International Monetary Fund, “Debt Relief under the Heavily Indebted Poor Countries (HIPC) Initiative”; World Bank, “Heavily Indebted Poor Countries (HIPC) Initiative”).

25 A recent and welcomed step was the willingness of China to address the debt burden of Ghana (The Economist, “China and the West take a step to ease Africa’s debt crisis”). See also Dauda Sembene, “International Financial Institutions an an Era of Great Power Competition.”

26 Executive Directors of the International Development Association, “Additions to IDA Resources.”

27 While this may free resources for lending to lower-income countries, it would mean that MDB portfolios could become skewed towards riskier borrowers.

28 From my own experience in chairing the board of an MDB executing unit of science and technology loans in Peru, complementary services allowed us to make effective use of the resources provided and to develop local capacities in higher education and in science, technology, and innovation. We were also able to benefit from the technical assistance of other countries in Latin America that had previously obtained loans from the IDB for similar purposes. Moreover, the legal standing of the loan contract allowed us to fend off interventions by outside parties that wanted access to these resources without following the rules agreed upon by the government and the IDB.

29 For an early review of the issues involved in the design of delivery systems and financing options for international and global public goods, see: Sagasti and Bezanson, Financing and Providing Global Public Goods. The annex to this paper contains an excerpt of this report that describes the design for an idealized global and international public goods delivery system. For proposals specifically aimed at the World Bank, see: Birdsall and Webster, “A GPG Window at the World Bank.”

30 Research and development expenditures of low- and middle-income countries in the late 2010s range between 0.44-0.69 percent of GDP, and for high-income countries, it averages 2.97 percent of GDP. While income per person was about 48 times lower in low-income than in OECD countries, indicators of scientific and technological output show a far greater disparity. For example, academic publications per 100,000 inhabitants in low-income-countries were about 100 times lower than in high-income countries (World Bank Open Data, “Research and Development Expenditure (% of GDP).” Moreover, considering the cumulative character of science and technology achievements, the fact that these disparities have been maintained for long periods of time suggests the difficulties in bridging gaps in knowledge capabilities.

31 For a recent review of the role of MDBs in the provision of international public goods, see: Oxford Economics, “Multilateral Development Banks for Global Public Goods.”

32 United Nations, “Our Common Policy Agenda Policy Brief 6: Reforms to the International Financial Architecture.”

33 The European Bank for Reconstruction and Development has allocated up to three billion euros for support to Ukraine during 2022-2023, and the European Investment Bank has approved an “EU for Ukraine” initiative that will support priority reconstruction and recovery investment in sectors identified by Ukraine, the World Bank, the European Commission, and the United Nations in the second Rapid Damage and Needs Assessment. See: Bennett, “EBRD Governors Support New

Financial Backing for the Bank" and European Investment Bank, "The EIB Stands with Ukraine."

34 "The World Bank and the Government of Iraq estimated losses from the war with the Islamic State in Iraq and the Levant (ISIL) at close to $46 billion, with needs resulting from the conflict totaling approximately $88 billion" (Islamic Development Bank, "The Road from Conflict to Reconstruction," Page 25.)

35 Asian Development Bank, "ADB Launches Integrated Approach."

36 See: African Development Bank Group, "Bank Group's Strategy."

37 A program in this field was spearheaded by the International Development Research Center of Canada for a decade. See: International Development Research Centre, "Think Tank Initiative."

38 Allan, "The Biden Administration." See also: The White House, "Remarks by National Security Advisor," and U.S. Department of the Treasury, "Remarks by Secretary of the Treasury."

39 For an idea on how this could be done in Latin America, see: Sagasti, "Hacia un Programa Regional de Cooperación en Ciencia."

40 Sagasti and Alcalde, Development Cooperation in a Fractured Global Order.

41 References can be found in the book this excerpt is drawn from.

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ABOUT THE AUTHOR

Dr. Francisco Sagasti is a fellow at the Woodrow Wilson International Center for Scholars in Washington DC; professor, Pacífico Business School in Lima Peru; and senior affiliated researcher at the Instituto de Estudios Peruanos. He has been President of the Republic, congressman and leader of his parliamentary caucus, and chair of the Science and Technology Committee in Congress. Previously he has been Chief of Strategic Planning at the World Bank; Chairman of the United Nations Advisory Committee on Science and Technology; visiting professor at the Wharton School at the University of Pennsylvania, the Instituto de Empresa, and the University for Peace; consultant to international public, private and non-profit organizations; Chairman of the Science and Technology Program at the Prime Minister's Office in Peru; member of the Board of Governors of the Canadian Center for International Development Research (IDRC) and other international organizations; and founder and former Executive Director of GRADE and of FORO Nacional Internacional, two leading Peruvian think-tanks. He holds engineering degrees from the Universidad Nacional de Ingeniería in Peru and Pennsylvania State University, and a PhD in operations research and social systems science from the University of Pennsylvania and has published more than 150 academic papers and 30 books. He has received the Paul Hoffmann award, created in honor of the administrator of the Marshall Plan and first UNDP director; the first Robert K. Merton award of the International Sociological Association, created to honor the memory of the pioneer of the sociology of science; and the Edgardo Habich award, created in honor of the founder of the National Engineering School of Peru in the 1870s.

Webpage: www.franciscosagasti.com

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Woodrow Wilson International Center for Scholars
Latin American Program
One Woodrow Wilson Plaza
1300 Pennsylvania Avenue NW
Washington, DC 20004-3027

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