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The World Bank as an International Financial Institution

ABSTRACT

The World Bank is a prestigious and large international financial institution. Since its foundation it has widened the scope and the size of its activities. One interpretation of what the World Bank is doing is the provision of public goods. If we take this interpretation seriously the comprehensiveness of the Bank's activity suggests that the Bank is assuming more and more the functions of a world government in the making. An alternative interpretation would look at the World Bank as a huge bureaucratic organization, acting on its own behalf. This interpretation can not be endorsed fully by the available information, but only in the sense of bureau-shaping. The Bank itself is proud of being a knowledge bank. But its actual activity is the popularization of ideas on development and not the application of research outcomes in its day-to-day operations. The most appropriate interpretation of the activity of the World Bank is that its changing scope and size is shaped heavily by pressure from different interest groups.

Keywords: international lending, economic development, public goods, interest groups

JEL-Classification: F33, F34, G21, O1

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1 Introduction

The World Bank is a prestigious and large international financial institution. The purposes of the World Bank are defined in the Articles of the Agreement. The normal assumption would be that the purposes of an institution can explain its actual activities. In the case of the World Bank we would expect that it lends the money it has raised on the world capital markets to its clients for the purposes of reconstruction and development. In this paper we will try to find out how far the World Bank meets these expectations.

Therefore, first of all we examine if there have been changes in the definition of the purpose and the kind of activity of the World Bank. If this is the case the question arises how to explain the size and the changing structure of the World Bank activity. We discuss four different theoretical approaches and examine in each case how far they help in understanding how the activities of the World Bank are shaped. The first approach is that of providing public goods discussed in part 2. In part 3 we draw upon the theory of bureaucracy for the same purpose. How far the activities of the World Bank can be explained by the assumption that it is a knowledge bank is discussed in part 4. Part 5 is devoted to the discussion of the theory of interest groups and its value in understanding the activities of the World Bank. In part 6 the question is raised if the Bank is still necessary. The conclusions are summarized in part 7.

2 Purpose and the Changing Activity of the World Bank

Article 1 of the Agreement of the International Bank for Reconstruction and Development specifies five purposes. These purposes are not tuned with each other in a coherent manner. The most familiar purpose is reconstruction and development, given in the first subsection. The other four purposes are mentioned less frequently in public and usually not discussed in the context of the activity of the World Bank. In several annual reports of the World Bank before 1989 the common objective of the World Bank group is mentioned to be "to help raise the standards of living in developing countries by channeling financial resources from developed countries to the developing world". But in the annual report of 1989 the central goal of the World Bank is given simply as "the reduction of poverty" (p. 38). Poverty reduction becomes from now on the most known short-cut for the objective of the World Bank. It is not easy to see if this small differentiation in defining the objectives of the World Bank makes a difference. That this can be the case is shown by the fact that in the 1970s a discussion started about the possible existence of a trade-off between the goals of output growth and equity for poor countries. McNamara, the then-President of the World Bank denied this (Kapur et al

1997, p. 16). But in terms of policy formulation the two different paraphrases of the goals may lead to diverse concepts with different implications for the development process. This can be observed looking at the changing activity of the World Bank since its foundation in 1944.

Initially the Bank concentrated on European recovery, not on the development of underdeveloped areas (Kapur and Webb 1996, p. 348). But its role in the reconstruction of Europe was minimal and soon the Bank began to reassess it, focussing on lending for development. The Bank began to borrow on the developed country capital markets and to re-lend for specific development projects (Toye 2003, p. 365), mainly in the fields of large-scale power and transport. Lending for agriculture was minor and for social sectors practically non-existent. Kapur and Webb (1996, p. 350) mention that this loan policy was considered to constitute a sound development strategy. Infrastructure investments were seen as an engine for growth, producing more private investments. Agriculture was seen as necessary but development was mostly identified with industrialization. Social sector expenditures (water, education and health) were avoided due to their high opportunity cost. It was in the 1970s that sectoral concerns (energy, agriculture, social sectors) won high priority. At the same time a poverty-oriented strategy was developed. McNamara, from the beginning of his Presidency in 1968, stressed the elements of a new approach to development: "the basic human needs". A greater share of the enlarged resources of the World Bank was, from now on, devoted to this new direction. He saw no trade-off between growth and poverty reduction. So Growth and Development, mentioned in Article 1 as the purpose of the World Bank, now became the indirect result of poverty orientation of the World Bank's activity.

At the end of the 1970s the serious problem of indebtedness of many developing countries arose following the two oil price shocks. This led to the rise of policy-based lending. This shift towards adjustment lending was based on conditionality. Funds would be released only as specific policies were implemented. The goal of adjustment lending was not poverty reduction, but to restore sustained economic growth. This led to a minor emphasis on poverty reduction during the first half of the 1980s. During the second half, poverty reduction once again became the central focus of the Bank’s policy. Even adjustment lending was developed into a more poverty oriented strategy. Adjustment lending had now the additional goal to protect the poor against adjustment shocks and to focus on the quality of life for the poor (Kapur et al. 1997, p. 29).

Today the specific focus of the World Bank is on poverty reduction. The vast activity of the World Bank in diverse areas is based on this interpretation of the main goal of the institution. Box 1 gives the major topic areas in which the World Bank is engaged.

Box 1: Major Topic Areas

Agricultural and Rural Development, Aids, Anti-Corruption, Debt Relief: Heavily Indebted Poor Countries, Education and Training, Energy, Environment, Evaluation Monitoring, Financial Sector, Gender, Globalization, Global Monitoring, Governance and Public Sector Reform, Health, Nutrition and Population, Information and Communication Technologies, Infrastructure, Knowledge Sharing, Law and Justice, Macroeconomics and Growth, Mining, Participation, Policies, Poverty, Private Sector Development, Social Development, Social Protection and Labor, Sustainable Development, Trade, Transport, Urban Development.

Source: World Bank Website

The entire list of topics is too long to be reported here. Examples for projects financed by the World Bank can be given for virtually every one of these topics, showing the comprehensive activity of this institution on every corner of our planet. Some examples showing the diversity and widely dispersed activity of the World Bank are given in box 2.

Box 2: Examples of World Bank Projects

Protecting street children in Turkey; How "Bollywood" music videos are boosting literacy, India; Shelter for the poor and housing, Iran; Building human capital for the global knowledge economy, Chile; Community kitchen, Argentina; Providing basic services to isolated villages, Yemen; Curbing HIV/AIDS, Burkina Faso; Restoring a marine ecosystem, Croatia; Legal titles to homeowners, Peru; Providing legal aid for poor women, Ecuador; Villagers get the chance to work again, Albania; Empowering citizens, Russia; Giving villagers a voice, Indonesia; Eliminating iodine deficiency, China; Bringing light to slums, Brazil; Restoring agriculture, Sri Lanka.

Source: World Bank Website

Looking at Article 1 of the Agreement and considering the differentiation in the definition of the goals of the World Bank since 1944 with its implication for the nature of its activity, one feels a great uncertainty about the true mission of the Bank and what has been the real object of its founders. Initially the World Bank was seen as a "development fund that would provide finance for clearly identified projects that would assist development" (Hughes 1999, p. 200). The lending concept was comparable to a commercial enterprise, financing projects proposed by its clients (Oliver 1996, p. 255).

But the Bank soon came to the conclusion that the borrowing countries lacked the technical expertise needed to prepare project application. It was also recognized that the soundness of projects ultimately rested on the overall quality of policy-making of the borrowing countries (Gavin and Rodrik 1995, p. 332).

Beyond lending activities the Bank entered therefore the realm of economic policy making. Sectoral and national economic reviews prepared by survey missions were introduced to investigate the over-all economic position of the borrowing country and probable investment resources. The World Bank also began to contribute to project appraisal and implementation (Hughes 1999, p. 201). As early as the end of the 1950s the Bank advised its clients to call in consultants to make the necessary preparations for a successful project and to look for organizations or individuals qualified to assist in running and implementing the project (International Bank for Reconstruction and Development, 1957, pp. 44-45). Today, far from it, the World Bank does not only dominate the whole project cycle but also, together with the IMF, the economic policy making in developing countries (for a description of the project cycle see box 3).

Box 3: Project Cycle

1. Country Assistance Strategy

The Bank prepares lending and advisory services, based on the selectivity framework and areas of comparative advantage, targeted to country poverty reduction efforts.

2. Identification

Projects are identified that support strategies and that are financially, economically, socially, and environmentally sound. Development Strategies are analyzed.

3. Preparation

The Bank provides policy and project advice along with financial assistance. Clients conduct studies and prepare final project documentation.

4. Appraisal

The Bank assesses the economic, technical, institutional, financial, environmental, and social aspects of the project. The project appraisal document and draft legal documents are prepared.

5. Negotiations and Board Approval

The Bank and borrower agree on loan or credit agreement and the project is presented to the Board for approval.

6. Implementation and Supervision

The borrower implements the project. The Bank ensures that the loan proceeds are used for the loan purposes with due regard for economy, efficiency, and effectiveness.

7. Implementation and Completion

The Implementation Completion Report is prepared to evaluate the performance of both the Bank and the borrower.

8. Evaluation

The Bank's independent Operations Evaluation Department prepares an audit report and evaluates the project. Analysis is used for future projects.

Source:

World Bank Website

3 The World Bank as a Provider of International Public Goods

Not only have there been changes in the definition of the purposes of the World Bank, but also in the size and structure of its activities. One interpretation of the changing activity of the World Bank could be its character as an international institution, providing international public goods. Initially, the rational explanation for the creation of the Bank was the imperfection of international capital markets. "Special risks", which the private lenders would not be ready to accept, were mentioned as the reason for the necessity of collective action to overcome this deficiency. Gavin and Rodrik (1995, p. 331) believe that "war and depressions clearly affect the returns on investment of all kinds, but it is far from obvious that they drive a wedge between private and public returns". If this was true private markets would have thrived soon after the war, so that there would not have been any argument for the creation of a World Bank. They mention further that it is " a little schizophrenic about an agency that preempts potential private lenders because they are allegedly too risk-averse, then demands that its loans be senior to any others, thereby shifting most of the risk onto private investors in unrelated projects, whose loans have thereby been subordinated." The argument of the imperfection of the international capital markets soon after the war would imply that the World Bank is only a temporary institution, the need for which would disappear as soon as the capital markets became more perfect (Gavin and Rodrik, p. 331-33).

The creation of the Bank is defended sometimes on the ground that there exists a "policy risk" making it necessary to have an impact on economic policy in developing countries (Gavin and Rodrik, p. 331). This is a justification for lending conditionality. But in this case also the same arguments apply. Private agencies could consult the developing countries on every aspect of economic policy making in a more appropriate way than the World Bank is presently doing. In the same manner it applies also that this function would have been temporary due to the learning capacity of developing countries.

In the literature the provision of public goods by the World Bank is not confined to overcoming the imperfection of the international capital markets and the policy intervening in the borrowing countries. Other public goods allegedly provided by the World Bank include (Stiglitz 1998, Gilbert et al. 2000):

Strengthening the democratic processes, promoting partnership with the private sector, providing knowledge about and relevant to development, global environment, correcting market failures, rectification of information failures, elimination of drug trafficking, management of global capital flows.

It is clear that a World Bank providing all these "public" goods would be a huge international organization, assuming roles that otherwise would be taken over by a world government. The question arises also, if private agencies could not provide such public goods. But it looks as if it is taken for granted that the World Bank is the appropriate organization to take on the provision of all kinds of public goods in the absence of a world government. It is surely a risky undertaking for the planet as a whole to transfer far-ranging responsibilities to an organization which was created for the simple job of canalization of capital to underdeveloped areas for development purposes, without any intention to reconfigure it to other directions. Such an organization will develop into an all-governing body while no conscious idea or deliberation would exist on the necessity and nature of such a world government in the making.

4 The World Bank as a Bureaucracy

Another interpretation of the World Bank activity is its character as a bureau, acting on its own behalf. "Bureaucrats are officials working permanently for large organizations in circumstances where their own contribution to organizational effectiveness cannot be directly evaluated" (Dunleavy 1991, p. 148). They are rational utility maximizers. There are two different interpretations of their maximization behavior. The basic approach is that officials maximize the size of the agency, which is assessed, as some writers suggest, primarily in terms of personnel. Another interpretation is that the agency's budget is the central focus for top officials. Larger budgets help bureaucrats push up salaries and fringe benefits, improve officials' promotion prospects and more easily divert resources into creating prestigious offices and more beautiful secretariats (Dunleavy 1991, p. 154-155).

Vaubel (1996) has analyzed the World Bank empirically as a bureaucratic organization. He writes that "international organizations are farther removed from democratic control than national government bureaucracies, and since their staff is recruited from highly diverse backgrounds, there is little else they can agree on but to pursue their common bureaucratic interest” (Vaubel 1996, p. 195). In his approach bureaucracies try to maximize their budget, their staff and their independence. In his empirical analysis he finds out that the growth of the staff of the World Bank has exceeded the growth of the staff in comparable institutions and that the labor productivity at the World Bank has declined since the 1950s and increasingly so since the 1970s (Vaubel 1996, p. 209). This means that the World Bank has suffered from bureaucratic deficiencies. But there are some weaknesses in the methodological approach of Vaubel (1996). First, calculating the productivity, the proxy for output, i.e. the number of credits approved during the financial year, is imperfect as he himself concedes (p. 196). It captures neither the quality of design of such credits nor of supplementary services. Taking this into account an annual increase of the ratio of staff to new credits of 0.4 percent can hardly be an indicator for declining productivity. Secondly, the adequacy of the growth of staff can only be judged relative to the task the respective organizations are asked to perform (Willet 2001, p. 329). Vaubel neglects this fact. His finding on the other side that the staff size in the World Bank is responsive to real labor cost (Vaubel 1996, p. 202) requires an explanation why this might be the case in a bureaucratized organization. Should this, however, not be the case it would contradict his bureaucratization thesis.

We present below some data which do not approve the thesis of bureaucratization of the World Bank as far as it is measured in terms of growing personnel or increasing administrative costs. As table 1 shows, the amount of loans approved by the World Bank and their disbursements have decreased recently in absolute terms. Table 2 shows that considering the growth rates, this has been the case since the mid-seventies. The highest growth rates are recorded for the 1960s until the mid-1970s. The same trend but with some outliner values is registered in the case of professional staff and administrative costs. This may also apply to the staff as a whole, presently around 10.000 persons.

This pattern can not be interpreted as an affirmation of the thesis of bureaucratization. There was a strong tendency towards bureaucratization at the beginning but this tendency became weaker in recent years. It may be that now a stalemate is reached and that the World Bank is neither continuing to grow nor is there any tendency towards shrinkage.

Table 1:
World Bank + IDA: The Record for 1960-2003, 5 Year Averages

in Million US$	1960	1965	1970	1975	1980	1985	1990	1995	2000
World Bank									
Loans approved	682	997	2.167	4.320	9.974	13.984	15.786	17.860	11.022
Disbursements	521	720	1.116	1.995	6.230	10.247	12.645	15.701	13.332
IDA									
Loans approved	195	288	928	1.576	3.384	3.809	5.908	6.434	6.618
Disbursements	64	281	369	1.026	2.095	3.146	4.197	5.765	5.177
Professional staff (no.)	360	691	1.487	1.883	2.631	3.392	-	-	-
Administrative costs	-	42	69	110	279	431	541	812	898

Source: The World Bank, Annual Report 1969-2003

Table 2:
World Bank + IDA: The Record for 1960-2003, 5 Year Averages, growth rates

Growth in %	1960	1965	1970	1975	1980	1985	1990	1995	2000
World Bank									
Loans approved	19	14	22	15	9	6	0	- 3	- 12
Disbursements	4	5	22	24	15	11	- 8	3	- 31
IDA									
Loans approved	36	53	26	5	- 3	13	9	2	6
Disbursements	189	- 4	51	22	13	9	12	- 2	- 8
Professional staff (no.)	12	19	10	10	3	6	-	-	-
Administrative costs	-	27	10	11	13	8	10	4	- 2

Source: Calculated from the World Bank, Annual Report 1969-2003

Dunleavy (1991) suggests another approach to the study of bureaucracy. For him the "characteristics of public service employment systems make it likely that the welfare of higher ranking bureaucrats is closely bound up with the intrinsic characteristics of their work rather than near-pecuniary utilities" (p. 209). Therefore bureau-shaping activities are the more adequate expression for the behavior of rational bureaucrats. Such activities are "designed to bring their agency into line with an ideal configuration conferring high status and agreeable work tasks, within a budgetary constraint" (p. 209). Bureaus cut down on routine workloads while maximizing the agency's policy control, they try to minimize its dependence upon external organizations, and export troublesome and costly low-grade tasks to rivals or to separated agencies (Dunleavy (1991, pp. 204-205). Seen from this perspective, in managing its loan portfolio and by advising developing countries (structural reform policies) and organizing costly trips for its staff around the planet for this purpose the World Bank looks to be a true bureau-shaping organization. This was especially true under Robert McNamara (1968-1981). The international reputation, the intellectual leadership and the financial clout of the bank were established during his term as president of the bank. He especially tried to maintain his independence and that of his institution from pressures from all sides (Clark 1981, pp. 178-182). But even today this bureau-shaping attitude can be felt clearly when contacting the different World Bank departments.

5 New Images: The World Bank as a Knowledge Bank

In 1996, the World Bank made a commitment to become a global knowledge bank. This might be another explanation for a series of activities of the World Bank during the last decade. To produce knowledge is of course not the goal of a bank. But the new image of the World Bank is just to do this, i. e. producing knowledge about development and disseminating it to the developing countries. This is justified with the character of knowledge as an international public good. Since no single country or private organization has the incentive to undertake the research necessary to create such knowledge, international institutions have to fill the gap (Squire 2000, p. 108-109). This is a curious argument due to the fact that many research institutes and organizations exist all over the world, producing exactly the kind of knowledge the World Bank is producing. Knowledge is non-rival but at least partially excludable and can therefore be produced and supplied privately. For the "knowledge that the developing world needs" (Squire 2000, p. 109) to be produced it is not therefore necessary that an international institution should solve "the difficult problem of coordinating the action of many countries" (Squire 2000, p. 109).

The necessity of in-house production of research is substantiated also by the argument that "it is difficult to structure incentives such that outside research institutes will deliver the kind of research the World Bank seeks to promote" (Squire 2000, p. 109). Apart from the fact that the kind of research which is produced in the World Bank is supplied by many institutions, nongratuitous research based on terms of reference is a very common way of producing knowledge and it is not clear why the World Bank should not be able to produce the knowledge it seeks using this approach. Gilbert et al. (2000, p. 50-51) believe that outside suppliers are not able to carry the requisite overhead costs. He compares the cost-minimizing pressures of such suppliers with the freedom of the

World Bank from such pressures due to its income on capital. But having no income constraint is a problem as far as it affects the quality of research negatively. In order not to waste resources, in case there is no income constraint, the production of knowledge should be outsourced.

As a primary rationale for an in-house research capacity at the World Bank Squire (2000, p. 109) names the necessity of integrating the results of research into the bank's everyday operations and making them available to policy makers in developing countries. This is of course an admissible reason for an in-house capacity. But how big should this capacity be? Squire (2000, p. 110) writes that judgement rather than quantitative measures drives the outcome. If this is the case the judgment has directed the bank towards gigantism in research. The bank has a very comprehensive research program (see box 4) and "remains the largest development research institution in the world" (Gilbert; Powell and Vines 2000, p. 49). This amount of research (1996 $ 25 million) cannot easily be justified by the necessity of integrating the results of research into day-to-day operations. For this purpose a much smaller research budget would be sufficient.

A report by the Operations Evaluation Department (OED) of the World Bank makes the above rational for an in-house research capacity even more questionable. It deserves to be cited at length (OED 2003, p. xii): "So far, the Bank's new activities consist primarily of knowledge aggregation and sharing - processes that by themselves do not guarantee that the shared knowledge will be adopted, adapted, and applied. For that to happen, knowledge sharing has to be embedded in work processes. But, for the most part, the new activities have not been tightly linked to the Bank's core lending and nonlending tasks. As a result, staff and clients do not view the new knowledge-sharing programs and activities as sufficiently relevant to their operational work".

Box 4: World Bank Research Topics

Agriculture	Industry	Public Sector Management
Domestic Finance	Infrastructure	Rural Development
Education	International Economics	Social Development
Environment	Labor & Employment	Transition Economies
Globalization	Macroecon & Growth	Urban Development
Governance	Poverty	Health & Population
Private Sector Development		

The comparative advantage of the World Bank does not lie in developing new and original ideas but in popularizing and spreading ideas developed elsewhere (Gavin and Rodrik 1995, p. 333; Gilbert; Powell and Vines 2000, p. 49). World Development Reports are examples of a comprehensive integration of results of research on special topics made inside and outside the bank. Ideas and even parlances popularized in these Reports are discussed and assimilated in a wide scientific and near-scientific community. This gives the World Bank the leadership in coining ideas on development. This leadership does not necessarily follow from the excellence of its research but it looks rather to be based on its large research capacity relegating all its competitors to the role of repetitors and admirers. It could even be the case that the research activity of the World Bank hinders the development of private research capacity in development elsewhere and especially in developing countries. These countries get the ideas delivered, so that any incentive to develop ideas and be curious about their own developing possibilities would be destroyed.

Where the World Bank could in fact serve the research community in an outstanding way is to redirect its available resources to and concentrate especially on the development and supply of comparative international data sets on development. This is the area where the real comparative advantage of an international institution like the World Bank lies, and where any other private organization or university will be hardly able to realize comparative standards. But it is not a virtue to use such data sets developed by the bank to test theories developed and propagated by the bank itself. This would lead easily into the temptation to manipulate data in order to find such theories empirically verified.

6 The World Bank and Interest Groups

Another interpretation of the World Bank’s activity would be to ask to what extent it is determined by the pressure of different stakeholders both inside and outside the bank with an interest in driving its activity to meet their own needs. The formal structure of the bank defines it as an agent executing the orders of its principal. The principals are in this case the member countries as shareholders represented by the Board of Governors, in whom all the powers of the Bank are vested. The agent is the management of the Bank represented by Executive Directors, to whom the Board of Governors has delegated all the powers over the conduct of the general operations of the Bank. In the decision-making process the power of each shareholder is exercised by the Executive Director representing it. The United States is the largest single shareholder, with 16.41 percent of votes, followed by Japan (7.87 percent), Germany (4.49 percent), the United Kingdom (4.31 percent), and France (4.31 percent). Every one of these five largest shareholders, as well as China, Saudi Arabia and the Russian Federation, appoints an Executive Director, while other member countries are represented as groups by the remaining 15 Executive Directors.

This picture of Executive Directors running the bank on behalf of the Board of Governors conveys a peaceful agent-principle relationship. In contrast, the initial stages of the bank were marked by an open conflict between the two. The first executive director for the United States Emillio Collado differed with the first president of the Bank Eugene Meyer over the size and speed of operations and especially over the balance of power between the Bank's management and its Executive Board. Collado favored an activist Board and saw the role of the president as implementing the Board's policy initiatives (Kapur et al. 1997, p. 10). Meyer resisted and resigned. McCloy, the next president managed to reach an agreement with the Board, making it a reactive body while the management would be in charge of all lending proposals and other operational initiatives (Kapur et al. 1997, p. 10).

This was the first time the World Bank stood up to defend its autonomy. The most influential president of the World Bank in this respect was Robert McNamara (1968-1981). Against the bank's rich shareholders he pressed aggressively the needs of the bank's underprivileged clients, while at the same time being quite careful to insulate himself from both recipient and donor politics (Kapur et al. 1997, p. 21). But this was not always successful. In the 1970s there has been constant pressure from the U.S. treasury and the congress to modify the bank's policy, which could not be resisted entirely. The Congress opposed especially the limited flow of information from the bank and the inadequacy of audit and evaluation systems. The bank was also pressed to keep salaries and benefits at levels comparable to those paid by private employers and the U.S. government.

The lending policy of the bank was also under attack (Gwin 1997, pp. 221-223). The Congress frequently expressed opposition to loans to particular countries. They especially targeted countries expropriating U.S. private property, socialist countries including Vietnam and countries violating citizens' human rights i. e. Chile. In addition, the Congress also objected to bank lending for the purpose of increase of production of commodities which could compete with U.S. commodities. The Congress was also influential in focussing the World Bank lending towards poverty alleviation. The pressure on the bank to increase the share of its assistance going to the poor and to put more emphasis on projects designed to meet basic human needs increased. In the report of the International Financial Institution Advisory Commission (Meltzer Report 2000), established by the Congress, poverty alleviation was again strongly recommended as the main focus of the World Bank.

We may conclude that one of the important factors determining the activity of the World Bank is the balance of power between the management of the bank and its largest shareholder, the U.S. The bank’s struggle for autonomy and the pressure by the U.S. to put through a policy according to its own interests are the two opposite forces forming the outcome. But this would be a simplistic view. The Congress has always provided multiple entry points for interest groups and they therefore also have an impact on the lending policies of the World Bank. From the 1970s on, church groups and private voluntary organizations began to lobby in opposition to a wide range of specific operations of the bank. These groups criticized the trickle-down theory of development. The bank came under attack for supporting regimes violating human rights and for not doing enough to aid the poor (Gwin 1997, pp. 211-212). Therefore liberal and conservative development groups in the U.S. had a decisive impact on the formulation of a pro-poor policy in the World Bank via Congress.

Another group with an impact on the lending policy of the World Bank is that of international commercial banks. For closer examination we have to look at the evolution of the policy-based lending in the World Bank. It is argued by Mosley et al. (1995) that the move towards policy based lending originated from within the operational divisions of the World Bank (Gilbert and Vines 2000, p. 22) due to the fact that these managers were disillusioned about the effectiveness of the project lending. Through policy-based lending it was possible that loan allocation was conditional on policy reforms in the recipient countries. The announcement of the new policy was made in 1979 in the wake of the international debt crisis. The crisis made it necessary to mobilize balance of payments support to indebted countries and the policy-based lending could also serve this purpose. The whole extent of the problem became clearer after the Mexican debt crisis broke out in mid-1982. Within the strategy developed by the U.S. Treasury and the Federal Reserve, the IMF and the World Bank played a central role. The strategy focused on rescuing the international commercial banks, to avoid outright default, avoid debt forgiveness and return the indebted countries to full debt service. The World Bank's new structural adjustment lending could therefore be used to rescue the international commercial banks and to advance market liberalizing and private sector policy reforms.

Structural adjustment lending had two functions. Program loans had to induce reforms and transfer resources to the borrower, enabling him to repay his debt. The second function proved to be much more important than the promotion of reform (Kapur et al. 1997, p. 22; Gilbert and Vines 2000, p. 23). Without new money it was impossible for the bank to participate in this process. The debt strategy evolved from the Mexican formula, to the Baker Plan of 1986, and the Brady Plan of 1989. International Monetary Fund and World Bank were authorized to channel new money to indebted countries. The United States supported an IMF quota increase in 1983, a $ 12 billion replenishment for IDA in 1987, and a doubling of Bank capital in 1988 (Kapur et al. 1997, p. 238). Both, right and left wings of the political spectrum in the Congress objected to "bailing out the banks" but the center bore up and the increase in new money was made possible. "Though the banks were not popular on Capitol Hill and could not take a high-visibility position on the quota increase, their behind-the scenes support was critical to the cause in Congress. Without the active support of the banks, it is doubtful that there would have been a Fund quota increase in the first half of the 1980s" (Henning 1996, p. 180). "Indeed, the Baker effect was to transfer major fractions of the commercial bank debt to the multilateral institutions" (Kapur et al. 1997, p. 31).

At the beginning of the 1980s, numerous other pressure groups entered the stage. The first-world nongovernmental organizations (NGOs) took on the bank as an adversary and pressed for a broadening of the policy agenda of the bank. The bank was under constant pressure to give these groups a say regarding the development of its policies. It was argued that the people and communities most affected by the bank’s policy were badly represented by their own governments on the board. The institution was therefore in need of "democratization", so as to better represent and be accountable to those it affects. The only way in which these people’s voice and concerns about bank projects could be heard would be for the bank to become more open and accountable to grassroots NGOs (Woods 2000, p. 148).

NGOs played a vital role in changing the bank policy. They were instrumental in prising the bank open, in increasing its transparency and accountability. "Poverty reduction" once again became the central mission of the bank. The adjustment agenda was broadened to include the protection of the poor against adjustment shocks and to include the quality of life for the poor into the macro-adjustment targets. For the bank, the most challenging agenda was that of environment, which was pushed by the NGOs. It included not only the health of natural environment but also the resettlement and the protection of indigenous people. Other issues were protection and improvements for women in development, and the furthering of the involvement of the bank in social sectors. "Governance" became a code word for varied issues ranging from defense expenditures by borrowing countries to human rights, combating corruption and political and administrative reform.

Politically especially the U.S.-based NGOs not only used informal channels of communication in the bank to propagate their views, they also grouped with anti-World Bank and anti-IDA forces in the Congress, which gave them a special impetus to enforce reforms comparing to other groups. Environment is a case in point. A coalition of environmentalists and fiscal conservatives in Congress pressed for environmental reforms at the bank. Withholding IDA replenishments served the Congress to force the bank to address environmental problems caused by projects it financed. From 1987 on the bank introduced environmental reforms (Nielson and Tierney 2003, pp. 260-265). A separate environmental Department was funded and the staff performing environmental assessments of projects increased to more than eighty persons. The number of environmental loans increased also. But the reforms could not satisfy the external critics. In 1992 the Congress threatened again to withhold the IDA replenishment unless the bank undertook serious and specific reforms. In 1994 the board of executive directors empowered an independent inspection panel to hear complaints from groups that would be directly affected by bank projects. Reporting requirements were enacted substantially opening records and documents to the public. Project managers were required to file, and periodically update, a public information document (PID). Each PID would contain a section devoted to "environmental aspects" of the project.

In this process, the board of executive directors could assert itself against the management, which reluctantly accepted the reforms. After 1993-94 the board managed to enforce changes to the loan approval process, which enabled the board members to be involved early in the planning stages of projects and to question or suggest changes to projects long before they reached the decision phase (Nielson and Tierney 2003, p. 264). The board insisted also on changes in the type of staff hired by the bank, so that the number of environmental scientists, economists and engineers employed increased dramatically between 1993 and 2000. They were involved in project planning, approval, and implementation. Since 1994 the board of executive directors received more timely and more detailed information about the environmental impact of bank projects.

The engagement of the World Bank with NGOs, now called civil society organizations (CSOs) had a profound impact on the World Bank organizational structure. The World Bank not only has established committees to hold regular meetings with the CSOs, but also has produced operational directives for staff on the need to reach out to civil society. The bank justifies its growing engagement with CSOs because engaging with them contributes to poverty reduction (World Bank 2003, p. 4). But the CSOs themselves look at the engagement of the World Bank in a different way. In a Bretton Woods Project text (2004a, p. 1) it is said that "Unofficially, the bank has no choice but to seek endorsement from increasingly powerful civil society actors to boost the legitimacy of its lending activities. From within the Bank however, there continues to be resistance to cementing this tenuous relationship; some staff question both the legitimacy of CSOs and the costs of engagement".

There are also fears on the side of CSOs. This came to the fore in the occasion of the first meeting of the Joint Facilitation Committee (JFC) in October 2003, which is a "joint World Bank- civil society working group committed to exploring transparent and effective mechanisms for dialogue and engagement between civil society and the World Bank at the global level". In a comment of the Bretton Woods Project (2004b, p. 2) to this event it is stated that "It remains unclear whether the JFC groups are poised to press the opportunities for strengthening the civil society voice and power in Bank operations while fending off dangers of co-optation" and further that "Whatever the promises, any institutionalized forum of large NGOs and the Bank will be in danger of resulting in photo opportunities and lowest common denominator generalities rather than empowerment of groups on the ground".

These fears of the CSO groups are not ill-founded looking at the way the World Bank is responsive to the criticism of these groups. Since the mid-1990s the bank hired civil society specialists to work in bank offices worldwide. Projected CSO involvement in Bank-funded projects increased from 21 percent of the total number of projects in 1990 to an estimated 72 percent in the fiscal year 2003 (World Bank 2004). Many of the civil society staff of the World Bank have worked in or lead CSOs before joining the World Bank. The World Bank has also established numerous funding mechanisms to provide grants to CSOs. It also has training programs available to CSO staff.

Our discussion in this section is summarized in table 3.

Table 3:
World Bank and Interest Groups

Group	Final goal	Means of pressure / Threatening power
Shareholders, especially U. S. congress and treasury (Board of executive directors)	Own global political preferences	IDA replenishment and Bank's capital increases
President/management of the Bank	Autonomy/bureau-shaping	Office
Professional staff	Bureau-shaping	lending power/ project management
Commercial banks	Bailing out	Informal contacts/ threatening of the collapse of the world financial system
NGOs/CSOs	Funding/jobs	Pressure on politicians/ criticizing

Source: Own compilation

According to this interpretation the activity of the World Bank anytime is the result of the pressure caused by different interest groups, which are in action at the time and the ability of the management to transform this pressure into operational directives. The outcome is not rational in the sense that goals are realized with given means. It is determined in a process of reaction, fending off, resisting, maneuvering and deciding. In this case any statement regarding the issue if the policy of the Bank is successful or not could itself easily become a subject matter to interest groups and hardly be settled by rigorous scientific analysis.

7 Is the Bank Still Necessary?

At the time of the creation of the World Bank there was a clear understanding that its role was the overcoming of the imperfections of the world capital markets. The Bank's second president John J. McCloy thought therefore that "the Bank was a temporary institution, the need for which would disappear as international capital markets became more nearly perfect" (Gavin and Rodrik, 1995, pp. 331-332). Today, the international capital markets are highly developed but the World Bank is far from being redundant. It has not only opened up new areas of activity in more advanced developing countries but has also become indispensable in poor developing countries. By refocusing its lending function and incorporating many new issues it is in a position to recommend its money and advice to every developing country in whatever situation. By this, it is demonstrating clearly that institutions, once created, develop their own life, eager to live and to expand and hopefully able to handle any external pressure they are exposed to.

Another development route would be opened if the Bank had to stick to its original role of being a bank. A bank lends money to a customer, who can present a sound project to be financed. It does not attach to the money it lends ideas and advice how to run the firm. In the case of the World Bank, in its early days the same procedure was applied. The institution was dominated by bankers (Gavin and Rodrik, p. 332). The soundness of a project presented by a sovereign customer depends of course on the overall quality of policy making. According to Gavin and Rodrik (1995, p. 332) this was one of the reasons why the Bank was required very early on to have ideas about what constituted an appropriate policy context. Conditionality became therefore part of the Bank's approach to lending, so that Bank money "always came with ideas and advice attached" (Gavin and Rodrik 1995, p. 333).

In the case of a commercial bank the soundness of a project depends also on the overall policy of the firm. The bank evaluates the overall policy of the firm but it does not prescribe policy instructions in detail to be followed by the firm. If the policy environment is not appropriate, the loan is denied or postponed as long as the firm has not changed its policies. In case of the World Bank it could be argued that a policy of conditionality is necessary because the borrowing countries lack the technical expertise to formulate and implement an appropriate policy. This argument might have been valid in the early days of the Bank. Today, in many cases the borrowers themselves are in a position to suggest policy reforms and if not, they may use the services of private firms and economic consultancies specialized on this kind of advice. In the case of the World Bank it is not clear why both functions i. e. comprehensive advice on practically all aspects of policy reforms and lending should be combined in one hand.

To return to its original function as a bank, therefore, the World Bank would have to concentrate on project appraisal, lending and monitoring the agreement continuously to ensure that the terms are followed and that all required payments are being made. Project preparation on the other hand, including preparing documents on the state of the current policies and the formulation of the required policy reforms, would be incumbent on the borrower, who can also use the services of specialized agencies. This division of responsibilities would have advantages for both, the Bank and the borrower. For the borrower the greatest advantage would be that of true ownership. The borrower has to formulate his own policy reforms and discuss them with the Bank. He is not confronted with an array of reforms he has to accept as a conditionality attached to the loan but he himself suggests reforms, he would be ready to implement if the loan was granted. The

Bank has also an impact on policy reforms while discussing the reforms suggested by the borrower. But it will be not the instance, felt as the one imposing reforms on the borrower.

Preparing and suggesting the required reforms on his own would also have an immense learning impact on the borrower. In order to get the loan the less developed borrower would have an incentive to learn about the pressing economic problems he wishes to overcome, the required reforms and how to present these reforms to the Bank attached to the Loan application. In discussion with the bank the borrower has to define his position. In this case the reforms are not imposed but agreed upon in a process of mutual understanding. For the borrower the process would be one of exercising oneself in policy formulation and policy making. Loans may be denied. But in this case the borrower has to learn to present a better reform project capable of being accepted.

There are also advantages for the Bank. First, the Bank will become more manageable and smaller. Second, much of the critique confronting the bank will recede and more important, the Bank will be much less subject to pressure groups.

8 Conclusions

The World Bank not only has widened the scope of its activity since its foundation but also its size. Today it is present practically in every corner of the planet with a multitude of diverse projects. It is not any more simply a bank lending money and earning interest, but an institution with a real impact on the economic policies of many developing countries. One interpretation of the World Bank’s activities is the provision of public goods. If we take this interpretation seriously the comprehensiveness of the Bank's activity suggests that the Bank is assuming more and more the functions of a world government in the making. An alternative interpretation would look at the World Bank as a huge bureaucratic organization, acting on its own behalf. This interpretation can not be endorsed fully by the available information but only in the sense of bureau-shaping. The Bank itself is proud of being a knowledge bank. But what the World Bank is really doing is popularization of ideas on development and not yet the application of research outcomes in its day-to-day operations. The most appropriate interpretation of the activity of the World Bank is that its changing scope and size is shaped heavily by pressure from different interest groups. It is struggling for autonomy but permanently subject to demands from diverse groups to change the nature and magnitude of its operations. It has to give way to these demands and in so doing the outcomes are shaped by compromise and not by rational action in the sense that goals are realized with given means.

The World Bank might have been better advised to return to its original plans of the 1950s and the beginning of the 1960s to confine its activity to the appraisal and approval of projects which are proposed by its clients. The other parts of the project cycle would be the business of the developing country and the consultants and private firms hired by the country. This is also true looking at the World Bank as an agency advising its clients to implement economic reforms. The World Bank could limit its activity to the appraisal of reform programs. The literal formulation and preparation of the reform program would then be the business of the developing country suggesting it for financing.

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