Testimony of Ian Solomon
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Chairman Kerry, Ranking member Lugar, members of the Committee, thank you for the opportunity to testify.

The World Bank is a critical partner in fighting poverty and promoting sustainable economic growth around the globe. As the Bank's leading shareholder for more than 65 years, the United States has helped shape the global development agenda, advancing maternal and child health, education, good governance, private sector growth, civil society, and responses to pressing global challenges such as food security, fragile states, and climate change, among other issues. Through U.S. investments in the World Bank, we have strengthened our policy objectives by helping to build a more peaceful and prosperous world.

Today I will discuss how continued U.S. support of the World Bank is vital to U.S. interests. I will address the World Bank's response to the financial crisis, the institution's request for additional capital, and how the United States is working with the institution to enact a robust reform agenda. I am pleased to be joined on this panel by Assistant Secretary of the Treasury, Marisa Lago, and by the United States Executive Director for the Asian Development Bank, Curtis Chin.

Response to the Economic Crisis

As Secretary Geithner remarked last week, this has been a terribly savage recession. In the United States and around the world, millions of people have lost their jobs, businesses large and small have shut down, families are struggling to regain their savings and livelihoods. Flows of private capital to developing countries dropped precipitously from a peak of $1.2 trillion in 2007 to $454 trillion in 2009, and estimates are that, due to the crisis, an additional 64 million people will fall into the ranks of extreme poverty, surviving on less than $1.25 per day. This has led some economists to estimate that 10 years worth of development gains in some world regions has been erased.

In early 2009, President Obama and other world leaders called on the World Bank to help shore up the global economy and protect the world's poorest by increasing lending in both middle-income and low-income countries. In response, the World Bank Group (WBG) -- comprising the International Bank for Reconstruction and Development (IBRD), the International Development Association (IDA), the International Finance Corporation (IFC), and the Multilateral Investment Guarantee Agency (MIGA) -- committed to triple its lending to over $100 billion over three years and to bolster anti-poverty efforts.

Given the depth of the crisis and the demand among developing countries for countercyclical lending, the World Bank exceeded this goal. It made $47 billion in commitments in FY09, $58.5 billion in FY10, and plans an estimated $33 billion in commitments for this year. Importantly, the Bank accelerated disbursements of funds to an unprecedented $80 billion in two years, more money than any other multilateral development bank (MDB). The World Bank was in a position to help address these extraordinary needs of developing countries thanks to years of sound financial management and accumulation of reserves.

Applying lessons from the Asian Financial Crisis and other financial crises, the Bank proved to be a strong partner in coordination with other donors and the IMF, focusing its response on its comparative advantages in protecting the vulnerable through support for social safety nets, supporting financing for infrastructure investment, and securing financial sectors to ensure credit for small and medium sized enterprises, which are vital engines of economic growth worldwide.

While we are still in the early days of assessing the World Bank Group's overall results, let me highlight a few examples. In Colombia and Mexico, the Bank supported conditional cash transfer programs, which expanded assistance to 2.7 million and 5.8 poor families respectively, through programs that promote school attendance and medical care for children. In Tanzania, the Bank provided interest-free credit to improve the access of the poor and vulnerable to job opportunities. In hard-hit regions of Central Asia, the Bank's infrastructure investments, which account for 29 percent of the overall increase in Bank commitments, improved regional transportation infrastructure. A clean energy project in Turkey helped reduce greenhouse gas emissions by an estimated 1.7 million tons of CO2 equivalents.

The IFC, with a focus on private sector investments, developed a $5 billion risk sharing mechanism through the Global Trade Liquidity Program (GTLP) to help build confidence between trade financiers who were concerned about counterparty bank risk. In one project, the GTLP supported a $100 million loan to a bank in South Africa to support trade in consumer goods, commodities, and small machinery in Africa. The IFC also launched a local currency bond to support lending to small and medium enterprises and strengthen capital markets in Central Africa, and developed a bank recapitalization fund to support banks of systemic importance.

MIGA, which provides political risk insurance, has been on the front line addressing financial sector vulnerabilities in Eastern and Central Europe by providing guarantees to key financial institutions in the region, helping to keep down borrowing costs and providing reassurance to banking regulators and investors.

For the poorest countries, the response by the WBG has also been rapid, though constrained by IDA's overall financing envelope, which is replenished every three years by donors. IDA is the multilateral fund to support the poorest people in the world and plays an essential role helping 79 low-income countries achieve sustainable growth and respond to both economic crises and natural disasters. IDA increased its lending by 25 percent and accelerated the pace of disbursements to provide appropriate fiscal support for countries. At the same time, the IFC increased its investments in IDA countries to almost 50 percent of all projects to catalyze additional private-sector growth and provide advisory services to improve the business climate.

These examples point to successes of the Bank's response, but we also know that there were areas of weakness as well. The World Bank's Independent Evaluation Group's (IEG) initial review of the crisis response noted that the Bank should have recognized the impact of the crisis earlier, and that in some cases, it underestimated the challenges associated with implementing new initiatives. Additionally, the Bank's analytical work in certain sectors and countries was uneven. Emerging lessons to be incorporated in the Bank's strategies going forward include: the continued importance of ensuring country ownership even in the face of global response in order to ensure the best results, the need to better anticipate crises in order to allow the Bank to intervene more effectively earlier and with better donor coordination, and the recognizing the value of the Bank's knowledge, which is generated through economic diagnostics and on-the-ground analysis, in helping the Bank and countries prioritize expenditures when resources are constrained.

The reach and effectiveness of the World Bank Group as demonstrated by its response to crisis and the ongoing recovery efforts underscore the importance of the Bank to advancing, in the words of President Obama, "the common security and prosperity of all people."

Investing for the Future: The Capital Increase

In responding to the crisis and helping fill the void created by the fall-off in private investment and government budgets, the World Bank stretched its historically strong balance sheet. As a result the Bank's equity to loan ratio, the traditional measure of the Bank's capital adequacy, is projected to fall below its prudential ratio of 23 percent starting in July 2013, unless some action is taken. The effect of this decline would be a drop in lending authority from an average of $15 billion a year in real terms before the crisis to less than $8 billion a year starting next year. This level would be less than a quarter of current projections for lending this year and is a small fraction of projected demand going forward.

To restore its capacity and better meet demand for its services, the Bank is seeking a 31 percent increase in capital, approximately $80 billion, through a number of measures, including increasing loan prices and securing shareholder contributions of both paid-in and callable capital. With a capital increase of this level, the Bank would have to scale back its elevated crisis lending to pre-crisis levels but could continue lending about $15 billion annually while sustaining its AAA credit rating. Without this capital increase, the Bank would need to sharply curtail its lending program.

The Administration supports the general capital and selective capital increases for the World Bank, which would require a contribution from the United States of $865 million over five years. This would be the first capital increase for the Bank since 1988, and would provide a highly effective way to advance several important policy objectives.

First, the U.S. contribution would be leveraged 55 times by the Bank and enable additional development lending of $48 billion over the next 10 years. The increase would enable the Bank to continue to assist countries in the fragile global recovery and to strengthen emerging and development markets for more balanced economic growth, including greater demand for U.S. exports.

Second, capital for the IBRD also secures support for IDA and the world's poorest. Every $1 contribution to capital will leverage close to $8 in income transfers from IBRD to IDA for a total of $6.6 billion IBRD income transfers to IDA over the next 10 years. Moreover, without the capital increase, annual IBRD support on which IDA has come to rely would be impossible to fund for years to come – placing a greater burden for IDA contributions on the shoulders of IDA donors. In this context, the upcoming IDA16 replenishment is a critical moment for not only shoring up IDA's capacity to help countries meet their development objectives but for building contingent support within IDA to enable a better and more robust crisis response capacity.

Third, the U.S. contribution to the capital increase will demonstrate U.S. support for the Bank's long term capital adequacy, which we believe is important for the Bank's AAA credit rating and the value of the U.S. capital in the IBRD.

Finally, and most importantly, the contribution will strengthen the Bank's capacity to complement U.S. bilateral programs and support U.S. policy priorities. Hence, there is no viable alternative to the capital increase without jeopardizing the Bank's credit rating, halving the size of the IBRD, and ending IBRD support to IDA. We want to continue to support the Bank's effective engagement throughout the development world. In particular, the Bank uses its global reach, expertise, strong fiduciary controls, and leverage to address many pressing global challenges, disseminate development knowledge and standards, and advocate sound economic and development policies at the country level. Some examples include:

> **Food Security.** After years of neglect by nearly all donors, the Bank has revamped its commitment to the agricultural sector through the Agricultural Action Plan that focuses on improving productivity gains, strengthening value addition, reducing risk and vulnerability of farmers, and enhancing environmental sustainability of agricultural practices. This renewed commitment is a strong complement to the recently launched Global Agricultural Food Security Program (GAFSP), a multidonor trust fund championed by the United States and other G20 members, that will catalyze investments in country-developed agricultural development plans. With the risk of another food price shock on the horizon, the Bank's experience from the 2008 food and fuel crisis provides timely assistance to the world's poorest countries to mitigate the shocks. For example, the Bank helped the Senegalese authorities implement a school feeding program. Similarly, Bank assistance in Nepal supported the supply of fertilizer, local seed development and small irrigation schemes for remote communities.
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> **Climate Change.** The United States has been at the forefront of pushing the World Bank to help countries develop low-carbon growth strategies with alternatives to traditional fossil-fuel based plans, and including climate issues in the Bank's country strategies. In recent years, the Bank has moved climate change from the periphery to the center of its mission to reduce poverty and support growth. The Bank's growing focus on climate is evident in three areas: 1) the development process itself; 2) financing, and, 3) knowledge and capacity building. This has translated into an 88 percent increase in renewable energy

and energy efficiency financing. In addition to its engagement with borrowing countries, the Bank has become a go-to source for research and data on climate and its impact on development.

Afghanistan. The United States has also benefited from the Bank's knowledge of working in fragile states. For example, in Afghanistan we turned to the Bank to set up the Afghanistan Reconstruction Trust Fund (ARTF) following the fall of the Taliban as a means to help meet the recurrent costs of running the government. The ARTF has expanded to support other national programs, such as the Afghan-owned and successful community-driven National Solidarity Program, which is helping communities build inclusive government through the selection and construction of development projects. Among other things, the ARTF leverages the Bank's comparative advantage as a fiduciary agent with strong financial management systems.

Governance, Accountability, Transparency. The U.S. relies on the Bank as a strong advocate of improving governance and transparency in developing countries. Its strong governance program not only gives us confidence that our aid dollars to the Bank are being used for the purposes intended, but also addresses the debilitating development challenge of corruption. For example, the Bank helped improve accountability mechanisms in Indonesia's Urban Poverty Program, which currently disburses about $100 million per year to over 8,000 villages across the country, through the election of 100,000 volunteers to serve as project overseers; the establishment of a website to report on implementation details, status of disbursement, details on project-related expenses; and a complaints-handling mechanism. The Bank also supports revenue transparency initiatives to promote government and private sector accountability through the Extractive Industries Transparency Initiative (EITI) and has recently launched the Stolen Assets Recovery (STAR) initiative to work with developing countries and financial centers to prevent the laundering of the proceeds of corruption and to facilitate more systematic and timely return of stolen assets.

Disaster Response and Recovery. The United States benefits from the Bank's repository of development knowledge and capacity to react quickly. In the wake of the devastating earthquake in Haiti and the rising flood waters in Pakistan, the United States called upon the Bank for advice on the response, to assess the needs, to strengthen local institutions, to help coordinate donors, and to help lead the reconstruction. The Bank has significant comparative advantages in this regard given its experience in events such as the 2004 Tsunami, 2005 Pakistan Earthquake, and numerous droughts and floods and other calamities throughout the years.

Private Sector Growth and Standards. Primarily through the IFC, the Bank plays a leading role helping to "crowd-in" private sector finance, and in a way that strengthens environmental and social safeguards. For example, IFC's performance standards ensure not only that IFC must operate at increasingly high levels of responsibility, but the standards have been adopted, following IFC's lead, by almost 70 private sector financial institutions. The "Equator Principles," as they are known, now govern the way many of the world's largest lenders measure and treat environmental and social sustainability.

Gender. Recognizing that inclusive growth is also smart growth, the Bank has been a leader in promoting economic opportunity for women. For example, in Tanzania by training commercial bank staff to better serve women entrepreneurs and enhance their financial literacy, women-owned small to medium sized businesses were able to access over $5 million in lending.

Ensuring the Effectiveness of U.S. Investments: Reform and Results

While the Bank continues to be an indispensable partner, it is also an institution in need of reform. This past Spring, Secretary Geithner said that "leverage alone is not sufficient to justify a substantial new financial commitment," rather it must be accompanied by "full implementation of a bold reform agenda, so that the world's leading development institution is vital and fully effective in meeting the challenges of the 21st century."

Recognizing the importance of a World Bank that is fully effective in meeting our challenges as well as the opportunity presented by the capital increase negotiations, the Administration increased its pressure for a robust set of reforms. Our persistence has been successful in the following ways:

First, the Bank has agreed to a unified financial framework to align financial decisions with the Bank's strategic priorities for the first time, enhance budgetary discipline, ensure loan prices cover costs, and create clear rules for transfers to IDA. The financial reform measures will help ensure that the Bank can be financially prepared for future crises with a sound and financially sustainable business model.

Second, we have emphasized the need for the Bank to be more open and accountable. In response the Bank has adopted a new access to information policy. This new policy will set the standard of best practice among global development institutions and help ensure the World Bank is transparent and accountable to all stakeholders. In addition, the Bank has moved to expand free access to its institutional knowledge and valuable development data through its OpenData initiative. The Bank is also piloting additional transparency innovations, including the use of geo-spatial mapping technology to illustrate the geography of investments made by the World Bank and other development partners alongside poverty and other demographic indicators.

Third, the Bank is improving its development effectiveness with increased attention on measuring and learning from results. This includes the commitment to develop a new compensation framework that will link performance to results, the creation of a corporate scorecard to improve management accountability for results, growing use of impact evaluation, and the expansion of the IDA Results Measurement System, which the U.S. championed, to the IBRD.

Fourth, the Bank developed a new strategy based on its comparative advantages, recognizing that it should not do everything and does not do everything best. The United States has been instrumental in helping to shape the strategic focus in alignment with our priorities, which includes: 1) Targeting the poor and vulnerable, especially in Sub-Saharan Africa; 2) creating opportunities for growth with a special focus on agriculture and infrastructure; 3) promoting global collective action on issues from climate change and trade to agriculture, food security, energy, water and health; 4) strengthening governance and anti-corruption efforts; and, 5) focusing on crisis response.

Commitments to reform have been made and progress in implementation has already been realized. Our task now is to stay vigilant and ensure vigorous implementation of the entire reform agenda.

Conclusion

A strong World Bank complements our government's capacity on development issues that demand attention. Nearly every day I receive requests from Treasury, the State Department, USAID, the National Security Council, the Commerce Department, USTR, and other agencies and government offices regarding work the World Bank is doing in countries from Afghanistan to Sudan, or on issues from fragile states to energy policy. We know that the World Bank's efforts can help us achieve our objectives, and our ongoing support of the institution ensures it.

After a long and careful review, the Administration determined that the general capital and selective capital increases are essential to the Bank's ability to work with us in effective partnership, both in recovery from crisis and on priority issues into the future. Not supporting the capital increase could jeopardize the Bank's credit rating, halve the size of the IBRD, and end IBRD support to IDA. We are confident that the package of capital and reforms will benefit all shareholders of the Bank, our interests, and especially the clients and beneficiaries of World Bank Group work across the developing world.

Finally, I take very seriously the responsibility to ensure that taxpayer resources are spent responsibly and seek to advance America's interests as effectively and efficiently as possible. In this regard, I am confident that the World Bank is a worthy and necessary investment of strong, continued support.

Thank You.